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TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1940

No. 242

**PHILADELPHIA COMPANY AND CERTAIN UNDER-
LIERS, PETITIONERS,**

vs.

**WALTER L. DIPPLE, JAMES P. McARDLE, BEN
PAUL BRASLEY AND THOMAS J. HOFFMAN,
ETC., ET AL.**

No. 243

**PHILADELPHIA COMPANY AND CERTAIN UNDER-
LIERS, PETITIONERS,**

vs.

**WALTER L. DIPPLE, JAMES P. McARDLE, BEN
PAUL BRASLEY AND THOMAS J. HOFFMAN,
ETC., ET AL.**

**ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT
OF APPEALS FOR THE THIRD CIRCUIT**

PETITION FOR CERTIORARI FILED JULY 15, 1940.

CERTIORARI GRANTED OCTOBER 14, 1940.

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[fol. 1]

**IN UNITED STATES DISTRICT COURT, WESTERN
DISTRICT OF PENNSYLVANIA**

RELEVANT DOCKET ENTRIES

1938

May 10. Filing fee \$110.00.

May 10. Petition of Pittsburgh Railways Company to effect a Plan of Reorganization filed. (C. M.)

May 10. Order made approving said petition as properly filed; directing that debtor continue in possession of its property; and fixing June 9, 1938 as time for hearing to determine whether debtor shall continue in possession or a Trustee appointed. (C. M.)

May 27. Proof of publication filed by debtor of filing of petition of May 10, 1938.

June 3. On petition of H. Fred Mercer, et al., order made authorizing H. Fred Mercer, Morris G. Levy, Walter L. Dipple and James P. McArdle, members of the committee known as "Tort Creditors Committee" to intervene generally in this proceeding on behalf of all other Tort Creditors who may join with said Committee.

June 8. Proof of service of notice of hearing fixed for June 9, 1938 filed Re: continuing debtor in possession or appointing Trustees, filed.

June 9. Hearing on the matter of appointment of Trustees before Judge McVicar. Hearing Memo. filed.

June 10. Hearing on matter of appointment of Trustees before Judge McVicar. Hearing Memo. filed.

[fol. 2] June 14. Order made appointing W. D. George, Thomas M. Benner, Esq., and Thomas Fitzgerald as Trustees for Pittsburgh Railways Company; they to file bond in the sum of \$100,000.00; directing that these proceedings be referred to Watson B. Adair, Esq., as Special Master; fixing September 14, 1938 as time on or before which claims shall be filed with said Special Master, provided that claims for damages based upon causes of action arising on or before August 1, 1938, may be filed within thirty days after entry of judgment thereon; Plan of Reorganization shall be filed by debtor on or before December 14, 1938. (C. M.)

June 15. Trustees' bond approved and filed—Pittsburgh

Railways Company (Globe Indemnity Company—\$100,000.00).

July 22. Amendment to order of Court dated June 14, 1938 for appointment of permanent Trustees for debtor filed by leave of Court.

Oct. 28. On petition, order made directing that the order of Court of June 3, 1938 be amended by adding thereto Ben Paul Brasley, Esq., and Thomas J. Hoffman, Esq., as members of the Tort Creditors Committee in these proceedings.

Nov. 7. On petition, order made directing that the appointment of Thos. Fitzgerald, as one of the Trustees of debtor shall be deemed to be an appointment of said Thos. Fitzgerald as an additional Trustee for the purpose of operating the business of the debtor in conjunction with the other Trustees; that the appointment of Thos. Fitzgerald as one of the Trustees of Subsidiary shall be deemed to be an appointment of said Thos. Fitzgerald as an additional Trustee for the purpose of operating the business in conjunction with the other Trustees; that all provisions of the Chandler Act shall henceforth apply to this proceeding; that W. D. George and Thomas M. Benner, two of the Trustees shall [fol. 3] file a plan of reorganization on or before June 1, 1939 or a report of their reasons why a plan cannot be effected as to the debtor and the Subsidiary that said Trustees give notice to creditors and stockholders.

Nov. 7. Answer of debtor and of Subsidiary to petition of Trustees Re: applicability of the Chandler Act with respect to plan of reorganization, filed.

1939

Jan. 9. Order made referring all matters, both as to the debtor and (to) the subsidiary, not reserved to the Judge by the provisions of Chapter X of the Chandler Act, to Watson B. Adair, Referee, to hear and determine same; provided that claims of creditors and interests of stockholders and objections thereto and the various other matters which were referred to a Special Master by paragraph 11 of order of Court of June 14, 1938, as amended, relating to Pittsburgh Motor Coach Company, are not hereby referred to the Referee, but the provisions of orders dated June 14, 1938, as amended, with respect to those matters shall remain in full force and effect.

March 10. Order made directing that the petition of trustees Pittsburgh Railways Company and Pittsburgh Motor Coach Company for instructions with respect to certain taxes of debtor and subsidiary be referred to Watson B. Adair, Special Master for hearing and report, hearing to be held March 28, 1939, at 10:30 A. M.

March 17. Proof of mailing notice of hearing to be held by Special Master on March 28, 1939 re: Instructions as to the payment of certain taxes filed.

Aug. 22. Special Master's Report on Petition of Trustees filed March 10, 1939 with Instructions with Respect to Taxes filed (C. M. 4); together with transcript of testimony taken at hearing; objections to the Tort Creditors Committee to [fol. 4] payment of taxes or tax items set forth in the petition of trustees filed March 10, 1939.

Aug. 24. Proof of mailing notice in re: Special Master's Report on Petition of Trustees for Instructions with Respect to Taxes filed.

Aug. 28. Order made directing that the date for hearing on petition of trustees and on the report of the Special Master re: taxes and on any exceptions filed to said report of Special Master be adjourned to Sept. 12, 1939 at 10 A. M.

Sept. 11. Exceptions Ex Parte Allegheny, Bellevue and Perrysville Railway Company, et al., to the report and recommendations of the Special Master on Petition of Trustees, filed March 10th, 1939, for instructions with respect to taxes, filed.

Sept. 11. Exceptions to the report and recommendations of Special Master filed March 10, 1939 for instructions with respect to taxes filed by the Trustees of debtor company filed.

Sept. 11. Exceptions and Objections of The Allegheny Traction Co. to Report of the Special Master in Re: Petition of Trustees for instructions with respect to payment of taxes, filed.

Sept. 12. Exceptions of Suburban Rapid Transit Street Railways Company to report of Special Master re: petition of trustees for instructions with respect to payment of taxes, filed.

Sept. 12. Exceptions of Citizens Traction Company to the Report of Special Master re: Petition of Trustees for Instructions with respect to payment of taxes, filed.

Sept. 29. Joinder of Samuel H. Putnam in exceptions to report and Recommendations of Special Master on Petition

of Trustees filed March 10, 1939, for instructions with respect to taxes, filed.

[fol. 5] Oct. 3. Hearing on Report of Special Master re: Petition for Instructions as to Payment of Certain Taxes held before Judge McVicar. Same day hearing concluded. (Hearing Memo. filed.)

Oct. 26. Opinion filed by Judge McVicar. Re:—Certain Taxes. (C. M. 4.)

Oct. 26. Order made directing that the Trustees pay certain taxes, together with any penalties and interest which may have accrued thereon; that the exceptions filed to the report of the Special Master, upon said petition be sustained in so far as they are in accordance with the provisions of this order and are dismissed in so far as they are not in accordance therewith. (C. M. 4.)

Oct. 28. Acceptance of service of decree and opinion re: payment of certain taxes filed. (2.)

Nov. 25. Notice of Appeal of Tort Creditor's Committee to the Circuit Court of Appeals filed.

Nov. 25. Bond on Appeal of Tort Creditors' Committee filed.

Nov. 25. Copy of Notice mailed to Circuit Court of Appeals.

Nov. 25. Copy of Notice mailed to attorneys for Appellee.

Nov. 25. Notice of Appeal of City of Pittsburgh to the Circuit Court of Appeals filed.

Nov. 27. Copy of Notice mailed to Circuit Court of Appeals.

Nov. 27. Copy of Notice of Appeal mailed to Attorneys for Appellee.

Nov. 27. Bond on Appeal of the City of Pittsburgh filed.

Dec. 11. On petition order made authorizing the City of Pittsburgh and the Tort Creditors Committee to print in the record on appeal from the order of Court of Oct. 26, 1939, directing the Trustees of the debtor company to pay certain taxes, only the docket entries set forth in Exhibit [fol. 6] "A" attached to petition, in lieu of the docket entries on the record except such other docket entries as the appellees may designate with the approval of the Court.

Dec. 11. Acceptance of service of notice as to printing the record on appeal filed.

Dec. 13. Statement of Appellants' (City of Pittsburgh and the Tort Creditors' Committee) Points on Appeal filed.

Dec. 13. Designation of Contents of Record on Appeal (City of Pittsburgh and Tort Creditors' Committee) filed.

Dec. 13. Transcripts of Testimony (2) taken March 28, 1939 at hearing on Petition of Trustees Respecting Taxes and Adjournments thereof, filed.

Dec. 14. Acceptance of service of notice of filing Designation of Contents of Record on Appeal and Statement of Points, filed.

Dec. 22. Recommendations of counsel for trustees relative to Trustees' Petition for Instructions with Respect to Certain Taxes filed.

Dec. 22. Designation of Additional Portions of the Record, proceedings and Evidence to be included in the Record on Appeal and Notice and Acceptance of Service filed.

Dec. 22. Order made directing that the time for filing of the record on appeal with the Clerk of the Circuit Court of Appeals in the appeals of the City of Pittsburgh and the Tort Creditors Committee from an order entered by this Court on Oct. 26, 1939 be extended from Jan. 4, 1940, to Jan. 18, 1940, provided that both the typewritten and printed record be filed on or before Jan. 18, 1940.

Dec. 22. On petition order made directing that there be filed and docketed in the office of the Clerk and made a part of the record in this proceeding the "Recommendation of [fol. 7] Counsel for Trustees Relative to Trustees Petition for Instructions with respect to Certain Taxes" which Blaxter, O'Neill & Houston filed with McVicar, J. personally on or about October 20, 1939, which document does not appear to have heretofore been filed and docketed in the office of the Clerk of this Court. Same day exception noted to City of Pittsburgh and Tort Creditors Committee.

Dec. 29 Stipulation of counsel as to additional portions of the record that shall be printed in the Record on Appeal in the appeals of the City of Pittsburgh and the Tort Creditors' Committee, filed.

IN UNITED STATES DISTRICT COURT

ORDER RE DOCKET ENTRIES

At Pittsburgh, in said District, this 11 day of December, 1939.

The foregoing petition having been presented in open

court, upon due consideration and on motion of counsel, leave is hereby granted to the City of Pittsburgh and the Tort Creditors Committee to print in the record on appeal from the order of court of October 26, 1939, directing the Trustees of Pittsburgh Railways Company, debtor within named, to pay certain taxes, only the docket entries set forth in Exhibit "A" attached to said petition, in lieu of the docket entries on the record except such other docket entries as the appellees may designate with the approval of the court.

By the Court, V.

[fol. 8] IN UNITED STATES DISTRICT COURT

PETITION OF TRUSTEES OF PITTSBURGH RAILWAYS COMPANY, DEBTOR, AND PITTSBURGH MOTOR COACH COMPANY, SUBSIDIARY, PRAYING FOR INSTRUCTIONS WITH RESPECT TO CERTAIN TAXES OF THE DEBTOR AND THE SUBSIDIARY—Filed March 10, 1939

To the Honorable, the Judges of Said Court:

The petition of W. D. George, Thomas M. Benner and Thomas Fitzgerald respectfully represents:

Pittsburgh Railways Company, Debtor

1. Your petitioners were, by Order of Court made June 14, 1938, appointed Trustees for Pittsburgh Railways Company, debtor, and they duly qualified and are now acting as such Trustees.
2. The said Order of Court made June 14, 1938 authorized your petitioners, inter alia, "to preserve, maintain, manage and operate and keep in good order, condition and repair, the property and estate in possession of and/or owned by the Debtor, and to manage and conduct its business; and without limiting the generality of the foregoing, to collect and receive the income, rents, revenues, tolls, issues and profits of said property and estate; * * * to pay all taxes and assessments due or to become due upon the property in possession of and/or owned by the Debtor."
3. At the time your petitioners were appointed Trustees for the debtor, the debtor was, and for many years prior

thereto had been, in possession of the street railway or in-
[fol. 9] cline plane properties of approximately 55 separate
companies, hereinafter referred to as underliers, which
properties the debtor managed and operated, in conjunc-
tion with the properties which the debtor owned, as the
Pittsburgh Railways Company transportation system.

A list of said underliers is shown on Schedule A hereto
attached.

4. The said underliers' properties were in the posses-
sion of the debtor under and pursuant to leases or operat-
ing agreements. The properties of approximately 80% of
the underliers were in the possession of the debtor under
either that certain Operating Agreement between Pitts-
burgh Railways Company and United Traction Company
dated January 1, 1902 or that certain Operating Agree-
ment between Pittsburgh Railways Company and Consoli-
dated Traction Company dated January 1, 1902.

Said leases and operating agreements required Pitts-
burgh Railways Company to pay, inter alia, the taxes of
the underliers, and prior to the institution of the reorgani-
zation proceedings, Pittsburgh Railways Company paid all
taxes of the underliers, including taxes of the kind here-
inafter referred to.

The following provision with respect to payment of taxes
appears in the said Operating Agreement between Pitts-
burgh Railways Company and United Traction Company,
and the identical provision also appears in the said Operat-
ing Agreement between Pittsburgh Railways Company and
Consolidated Traction Company except the word "Con-
solidated" appears in place of the word "United":

"Pittsburgh (Pittsburgh Railways Company) agrees
to pay all expense of operation and ordinary maintenance
of the lines of railway leased, owned and operated by United;
[fol. 10] also to pay all State, County or Municipal taxes
assessed against United or which by any present or future
law or by contract United may be required to pay; * * *"

Your petitioners are informed and believe that said
United Traction Company was required by contract to pay,
with respect to the underliers in the so-called United Traction
Group, taxes of the kind hereinafter referred to, and
Consolidated Traction Company was required by contract
to pay, with respect to the underliers in the so-called Con-

solidated Traction Group, taxes of the kind hereinafter referred to.

5. Your petitioners have neither affirmed nor disaffirmed any of the leases or operating agreements under and pursuant to which the properties of the underliers came into the possession of the debtor.

6. The debtor and each of the underliers listed on Schedule A are required to file with the Commonwealth of Pennsylvania, on or before March 15, 1939, a Capital Stock Tax Report for the calendar year 1938, pursuant to the provisions of the Act of June 1, 1889, P. L. 420, as amended (72 PS, 1871).

The tax due on said report is payable when the report is due. (Act of April 9, 1929, P. L. 343, as amended—72 PS, 707.)

7. The debtor and each of the underliers listed on Schedule A are required to file with the Commonwealth of Pennsylvania, on or before March 15, 1939, a Corporate Loans Tax Report for the calendar year 1938, pursuant to the provisions of the Act of June 30, 1885, P. L. 193, as amended (72 PS, 2162).

[fol. 11] The tax due on said report is payable when the report is due. (Act of April 9, 1929, P. L. 343, as amended—72 PS, 708.)

8. The debtor and each of the underliers listed on Schedule A are required to file with the Commonwealth of Pennsylvania, on or before April 15, 1939, a Corporate Net Income Tax Report for the calendar year 1938, pursuant to the provisions of the Act of May 16, 1935, P. L. 208, as amended (72 PS, 3420a).

One-half of the tax due on this report is payable when the report is due and the balance within thirty days after the report is due.

9. The aforesaid Capital Stock tax, Corporate Loans tax and Corporate Net Income tax bear interest at the rate of 6% per annum from the date they are respectively due until sixty days after settlement, and thereafter at the rate of 12% per annum until paid. (Act of April 9, 1929, P. L. 343, as amended—72 PS, 806.)

10. The debtor and each of the underliers listed on Schedule A are required to file, on or before March 15, 1939, a

Federal Income Tax Return for the calendar year 1938, pursuant to the provisions of the Federal Revenue Act of 1938. The tax becomes due March 15, 1939 but may be paid in quarterly installments beginning with that date; and in the event of default in payment of any installment, the entire balance of tax becomes immediately due and payable and bears interest at the rate of 6% per annum from the date of default.

11. The amounts of the aforesaid Pennsylvania Capital Stock tax, Corporate Loans tax, Corporate Net Income tax and Federal Income tax, due by the debtor and each of the underliers, as computed in accordance with the valuations [fol. 12] used for the calendar year 1937, are shown on Schedule A.

12. The Corporate Loans tax shown on Schedule A to be due by the debtor and certain of the underliers, in the total amount of \$28,717.35, is based upon interest paid by Pittsburgh Railways Company, prior to May 10, 1938, on its obligations and those of the underliers, and interest paid by your petitioners, subsequent to May 10, 1938, on the debtor's Car Trust Certificates. Of said total tax of \$28,717.35, the amount of \$772.00 represents the tax based on interest paid by your petitioners subsequent to May 10, 1938 on the debtor's Car Trust Certificates. Of said total tax of \$28,717.35, the sum of \$484.00 represents moneys withheld from the holders of the obligations for the purpose of paying the tax, and of said amount of \$484.00 the sum of \$182.00 represents the moneys withheld by petitioners in connection with the interest paid by them subsequent to May 10, 1938 on the debtor's Car Trust Certificates.

13. The Act of April 9, 1929, P. L. 343 (72 PS, 1401), the Fiscal Code, as last amended by the Act of June 11, 1935, P. L. 303 (72 PS, 1401), provides, in part:

"All State taxes imposed under the authority of any law of this Commonwealth, now existing or that may hereafter be enacted, and unpaid bonus, interest, penalties, and all public accounts settled against any corporation, association, or person, shall be a first lien upon the franchises and property, both real and personal, of such corporation, association, or person, from the date of settlement, and whenever the franchises or property of a corporation, association, or person shall be sold at a judicial sale, all taxes, interest,

bonus, penalties, and public accounts due the Commonwealth [fol. 13] shall first be allowed and paid out of the proceeds of such sale before any judgment, mortgage, or any other claim or lien against such corporation, association, or person * * *"

Taxes due the Commonwealth of Pennsylvania have, by statute, been made a lien on the taxpayer's properties from as early as the Act of 1811, 5 Sm. L. 228, Section 12, and the provisions of that section have remained in force and, with revisions, were carried into Section 1401 of the Fiscal Code aforesaid.

14. Substantially all the properties of the debtor and substantially all the properties of each underlier are subject to the lien of one or more mortgages, but none of said mortgage liens, so far as known by your petitioners, was created prior to the enactment of the aforesaid Act of 1811.

15. The Act of Congress of June 18, 1934, c. 585 (28 U. S. C. A. 124a), provides, in part, as follows:

"Any receiver, liquidator, referee, trustee, or other officers or agents appointed by any United States court who is authorized by said court to conduct any business, or who does conduct any business, shall, from and after June 18, 1934, be subject to all State and local taxes applicable to such business the same as if such business were conducted by an individual or corporation * * *"

16. For the calendar year 1939 the debtor will be required to file periodic reports and pay the taxes becoming due thereon pursuant to the Pennsylvania Unemployment Compensation Law, approved Dec. 5, 1936 (1937, P. L. 2897; 43 PS, 751), and pursuant to Titles VIII and IX of the Federal [fol. 14] Social Security Act of August 14, 1935 (42 U. S. C. A. 1001 and 1101).

Payments under the State Unemployment Compensation Law and payments under the Federal Old Age Benefits tax (Title VIII) are due quarterly on the last day of the month following the close of the calendar quarter, and payments under the Federal Unemployment Insurance Tax (Title IX) are due on the last day of the month following the calendar year. Credit is allowed on the last named tax in the amount of 90% of the tax paid under the State Unemployment Compensation Law.

The State Unemployment tax bears interest at the rate of 1% per month from the date it becomes due until paid.

The Federal Old Age Benefits tax and the Federal Unemployment Insurance tax bear interest at the rate of $\frac{1}{2}$ of 1% per month from the date they become due until paid.

The aforesaid taxes, commonly called "Social Security Taxes," are based on wages paid by employers to employes, and under the express provisions of the Acts or rulings thereon, Trustees in Bankruptcy are considered employers for the purposes of the tax. These taxes are in connection with the employes of the debtor—they do not concern the underliers of the debtor.

17. The United States has filed liens against the debtor and certain of the underliers for Federal taxes pursuant to the provisions of Section 3186 of the Revised Statutes (26 U. S. C. A. 1560) as set forth on Schedule B hereto attached. The lien filed against the debtor is with relation to Federal Income taxes due for the years 1930, 1931 and 1932, and the lien filed against certain of the underliers is for Federal Income tax due for the calendar year 1937.

[fol. 15] Said Section 3186 of the Revised Statutes reads as follows:

"If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, penalty, additional amount, or addition to such tax, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person."

18. The United States has filed claims in this proceeding against the debtor for Federal taxes in large amounts.

Section 3466 of the Revised Statutes (31 U. S. C. A. 191) provides, in part, as follows:

"Whenever any person indebted to the United States is insolvent, or whenever the estate of any deceased debtor, in the hands of the executors or administrators, is insufficient to pay all the debts due from the deceased, the debts due to the United States shall be first satisfied * * *"

19. The following explanation is made of the arrangement of Schedule A. For the purposes of the Federal Income tax (and therefore also for the State Corporate Net

Income tax), a parent street railway company may file a consolidated return for itself and those subsidiaries in which it owns 95% or more of the stock. Schedule A is set up on that basis. Pittsburgh Railways Company owns at least 95% of each of the companies indented under its name on said Schedule; Consolidated Traction Company owns at least 95% of the stock of the companies indented under its name; and so on, throughout the Schedule.

[fol. 16] 20. In a budget for the debtor which your petitioners filed in Court on November 7, 1938 in connection with their application for authorization to make certain renewals, replacements and improvements to the properties in their possession, and which covered the period June 1, 1938 to May 31, 1939, provision was made, in the approximate amount of \$66,000, for Pennsylvania Capital Stock tax accruing against the debtor and underliers during the budget period as a tax assignable to street railway operation.

Under "Income Deductions" in said budget are included Federal Income tax in the approximate amount of \$127,000, State Income tax in the approximate amount of \$54,000, and Corporate Loans tax in the approximate amount of \$72,000, but while said items have been accrued for the budget period, provision for the payment thereof under the budget estimate has not been made, as said taxes would only arise and become payable if the Trustees of the debtor should, during the budget period, pay interest on the bonded indebtedness of the debtor and interest and rentals under leases and operating agreements hereinabove referred to.

In the aforesaid budget covering the period June 1, 1938 to May 31, 1939, provision was made, as taxes assignable to street railway operation, for State Unemployment tax and Federal Unemployment tax in the approximate total amount of \$163,000; and for Federal Old Age Benefits tax in the approximate amount of \$54,000, accruing during the budget period.

21. Petitioners had cash on hand, as of March 8, 1939, in the amount of \$1,537,247.46, or sufficient to pay any or all of the taxes hereinabove discussed if petitioners are instructed to make such payments. On May 10, 1938, the date of the filing of the debtor's petition herein, the debtor had cash on hand in the amount of \$230,260.00.

[fol. 17] 22. None of the underliers has funds with which to pay any of the taxes herein discussed which are applicable to it.

23. On March 15, 1938, Pittsburgh Railways Company paid the installments of Federal Income tax due March 15, 1938 on the return of Pittsburgh Railways Company and on the returns of the underliers for the calendar year 1937. Your petitioners have not paid nor, to their knowledge, has anyone paid the remaining installments which became due on account of said taxes.

Pittsburgh Motor Coach Company, Subsidiary

24. Your petitioners were, by Order of Court made June 14, 1938, appointed Trustees for Pittsburgh Motor Coach Company, subsidiary, and they duly qualified and are now acting as such Trustees.

25. The said Order of Court made June 14, 1938 authorized your petitioners, inter alia, "to preserve, maintain, manage and operate and keep in good order, condition and repair, the property and estate in possession of and/or owned by the Subsidiary, and to manage and conduct its business; and without limiting the generality of the foregoing, to collect and receive the income, rents, revenues, tolls, issues and profits of said property and estate; * * * to pay all taxes and assessments due or to become due upon the property in possession of and/or owned by the Subsidiary."

26. Pittsburgh Motor Coach Company, subsidiary, is required to file with the Commonwealth of Pennsylvania, on or before March 15, 1939, a Capital Stock Tax Report for the calendar year 1938, and the amount of the tax as computed by your petitioners will be the sum of \$5.00, as shown on Schedule A. The said tax will become due and payable when the report is due. While the subsidiary will be re-[fol. 18] quired to file a Corporate Loans Tax Report, Corporate Net Income Tax Report and Federal Income Tax Return, it appears no tax will be due on account of any of them.

27. For the calendar year 1939, Pittsburgh Motor Coach Company, subsidiary, will be required to file periodic reports and pay the taxes becoming due thereon pursuant to the State Unemployment Compensation Law and pursuant to Titles VIII and IX of the Federal Social Security

Act imposing Federal Unemployment Insurance tax and Federal Old Age Benefits tax respectively, as hereinbefore in paragraph 16 more fully referred to.

In a budget for the subsidiary which your petitioners filed in Court on January 30, 1939 in connection with the application of your petitioners, as Trustees of the debtor, to pay operating losses of and to make loan to the subsidiary, and which covered the period June 1, 1938 to May 31, 1939, provision was made under operating expenses and taxes, for State and Federal Unemployment taxes in the approximate amount of \$14,500, and Federal Old Age Benefits tax in the approximate amount of \$4,800.

28. Prior to May 10, 1938, the date of filing of the debtor's petition herein, Pittsburgh Motor Coach Company became liable for the payment of Federal Old Age Benefits tax for the quarter ending March 31, 1938, imposed pursuant to Sections 801 and 804 of Title VIII of the Social Security Act of August 14, 1935 (42 U. S. C. A. 1001 and 1004). In payment of said tax, on or about April 27, 1938, Pittsburgh Motor Coach Company issued to the Collector of Internal Revenue its check in the amount of \$1,798.53, but the said check was not presented for payment prior to May 10, 1938, and when the same was presented payment thereof was refused. Thereafter, on July 28, 1938, your petitioners, as Trustees for Pittsburgh Motor Coach Company, subsidiary, paid the tax on employes imposed [fol. 19] under Section 801 of said Act in the amount of \$899.26, for the reason that said amount had been deducted from wages paid to the employes, but your petitioners did not pay, and have not paid, the tax on the employer imposed under Section 804 of said Act, and the said tax in the amount of \$899.26 remains unpaid. The said tax bears interest at the rate of $\frac{1}{2}$ of 1% per month from the date the tax became due until paid.

29. The United States has filed a lien against the subsidiary, pursuant to the provisions of Section 3186 of the Revised Statutes (26 U. S. C. A. 1560), for Federal Income taxes for the years 1930, 1931 and 1932, as set forth on Schedule B.

30. The United States has filed claims in this proceeding against the subsidiary for Federal taxes in large amounts.

31. Petitioners, as Trustees of the subsidiary, had cash on hand, as of March 8, 1939, in the amount of \$32,979.67, or

sufficient to pay any or all of the taxes hereinabove discussed, applicable to the subsidiary, if petitioners are instructed to make such payments. On May 10, 1938, the date of the filing of the subsidiary's petition herein, the subsidiary had cash on hand in the amount of \$29,558.00.

Wherefore, your petitioners, being in doubt as to whether or not they should pay any or all of the taxes hereinabove discussed, respectfully pray your Honorable Court to instruct them as to what action they should take with respect to payment of the following:

Debtor and Underliers:

(a) Pennsylvania Capital Stock tax of the debtor for the calendar year 1938.

[fol. 20] (b) Pennsylvania Corporate Loans tax of the debtor for the calendar year 1938.

(c) Pennsylvania Corporate Net Income tax of the debtor for the calendar year 1938.

(d) Federal Income tax of the debtor for the calendar year 1938.

(e) Pennsylvania Unemployment Insurance tax, Federal Unemployment Insurance tax and Federal Old Age Benefits tax of the debtor for the calendar year 1939.

(f) Pennsylvania Capital Stock taxes of the underlying companies in the debtor's transportation system for the calendar year 1938.

(g) Pennsylvania Corporate Loans taxes of the underlying companies in the debtor's transportation system for the calendar year 1938.

(h) Pennsylvania Corporate Net Income taxes of the underlying companies in the debtor's transportation system for the calendar year 1938.

(i) Federal Income taxes of the underlying companies in the debtor's transportation system for the calendar year 1938.

(j) Unpaid balance of Federal Income tax of the debtor for the calendar year 1937.

(k) Unpaid balances of Federal Incomes taxes of certain underlying companies in the debtor's transportation system for the calendar year 1937.

Pittsburgh Motor Coach Company, Subsidiary:

(l) Pennsylvania Capital Stock tax of the subsidiary for the calendar year 1938.

(m) Pennsylvania Unemployment Insurance tax, Federal Unemployment Insurance tax and Federal Old Age Benefits tax of the subsidiary for the calendar year 1939.

(n) Federal Old Age Benefits tax (employer's share) of the subsidiary which became due and payable April 30, 1938 for the quarter ending March 31, 1938.

W. D. George, Thomas M. Benner, Thomas Fitzgerald, Trustees.

Pittsburgh Railways Company System

Statement of Federal and State Tax Liability for the Year 1938
To Be Paid in the Year 1939

Pittsburgh Railways Company and Subsidiary and Affiliated Street Railway Companies (controlled through stock ownership)	Actual Liability		Estimated Liability	
	State Capital Stock Tax	Corporate Loans Tax See Note A	Federal Income Tax	State Income Tax
Pittsburgh Railways Company.....	\$5.00	\$11,214.79(B)	None	None
Allegheny, Bellevue and Perryville Railway Company.....	5.00	None	"	"
The Allenport and Roscoe Electric Street Railway Company.....	5.00	"	"	"
Ben Avon and Emsworth Street Railway Company.....	5.00	"	"	"
Bon-Air Street Railway Company.....	5.00	"	"	"
Cedar Avenue Street Railway Company.....	5.00	"	"	"
East McKeesport Street Railway Company.....	5.00	"	"	"
Glenwood and Dravosburg Electric Street Railway Company.....	5.00	"	"	"
The McKeesport and Reynoldton Passenger Railway Company.....	5.00	"	"	"
Mt. Washington Street Railway Company.....	5.00	"	"	"
Mt. Washington Tunnel Company.....	5.00	"	"	"
Pittsburgh, Allegheny, and Manchester Passenger Railway Company.....	5.00	"	"	"
The Pittsburgh, Allegheny and Manchester Traction Company.....	5.00	64.60	"	"
Pittsburgh & Charleoi Street Railway Company.....	5.00	None	"	"
Pittsburgh and West Eld Railway Company.....	5.00	"	"	"
Pittsburgh, Canonsburg and Washington Railway Company.....	5.00	934.80	"	"
Pittsburgh, Crafton and Mansfield Street Railway Company.....	5.00	60.80	"	"
Pittsburgh, Neville Island and Coraopolis Railway Company.....	5.00	None	"	"
Pittsburgh Union Passenger Railway Company.....	5.00	"	"	"
Second Avenue Passenger Railway Company.....	5.00	"	"	"
Second Avenue Traction Company.....	5.00	433.20	"	"
The Second Avenue Traction Company.....	5.00	None	"	"
Superior Avenue and Shady Avenue Street Railway Company.....	5.00	"	"	"
United Traction Company of Pittsburgh.....	5.00	6,408.89	"	"
Washington and Canonsburg Railway Company.....	5.00	1,266.80	"	"

EXHIBIT "A" TO PETITION—Continued

Pittsburgh Railways Company System

Statement of Federal and State Tax Liability for the Year 1938
To Be Paid in the Year 1939

Pittsburgh Railways Company and Subsidiary and Affiliated Street Railway Companies (controlled through stock ownership)	Actual Liability		Estimated Liability	
	State Capital Stock Tax	State Corporate Loans Tax See Note A	Federal Income Tax	State Income Tax
West End Traction Company	\$5.00	\$3,069.32	"	"
West Liberty and Suburban Street Railway Company	5.00	832.20	"	"
West Shore Electric Street Railway Company	5.00	None	"	"
Consolidated Traction Company	16,062.35	"	"	"
Arthore Street Railway Company	5.00	1,163.84	"	"
Central Passenger Railway Company	5.00	34.20(C)	"	"
The Central Traction Company	1,873.16	13.30	"	"
Fort Pitt Traction Company	5.00	None	"	"
The Pittsburgh Traction Company	4,187.50	22.80	"	"
The Duquesne Traction Company	1,499.27	171.00	944.50	443.63
The Duquesne Street Railway Company	5.00	None	None	None
Federal Street and Pleasant Valley Passenger Railway Company	2,683.75	2,486.26	409.82	145.17
The Morningside Electric Street Railway Company	5.00	None	None	None
Seventeenth Street Incline Plane Company	5.00	"	"	"
Total Inside Control	\$26,476.03	\$28,176.80	\$ 1,354.32	\$588.80
Other Street Railway Companies, a Majority of Whose Stock is Held by Outside Interest (operated by lease)				
Allegheny Traction Company	\$985.31	None	\$1,778.31	\$802.17
Millvale, Etna and Sharpesburgh Street Railway Company	5.00	\$3.80	None	None
The Citizens Traction Co.	7,495.64	38.00	232.25	113.80
Penn Street Railway Company	5.00	59.85	None	None
Monongahela Street Railway Company	17,500.00	None	27,447.50	9,577.10

Mount Oliver Incline Railway Company.....	375.00	157.70	109.25	53.53
Pittsburgh and Birmingham Traction Company.....	7,482.59	22.80	12,941.80	4,525.82
The Birmingham, Knoxville and Allentown Traction Company.....	5.00	None	None	None
Brownsville Avenue Street Railway Company.....	5.00	"	"	"
Pittsburgh and Birmingham Passenger Railroad Company.....	5.00	"	"	"
The South Side Passenger Rail Road Company.....	5.00	15.20	"	"
West Liberty Street Railway Company.....	5.00	None	"	"
Pittsburgh Incline Plane Company.....	800.00	"	2,085.95	934.46
The Suburban Rapid Transit Street Railway Company.....	3,150.00	243.20	4,912.00	1,740.04
Total Outside Control.....	\$37,823.54	\$540.55	\$49,507.06	\$17,746.92
Grand Total.....	\$64,299.57	\$28,717.35	\$50,861.38	\$18,335.72
Pittsburgh Motor Coach Company.....	\$5.00	None	None	None

Notes "A" Denotes liability for Corporate Loans Tax on bond interest paid by Pittsburgh Railways Company.

"B" A portion of this tax was withheld from coupon interest payments to taxable holders of Pittsburgh Railways Co. Car Trust 6% Series B Gold Bonds.

"C" All of the tax on Central Passenger Railway Company First Mortgage 6% Bonds was withheld from interest payments to the taxable holders.

Accounting Department,
Pittsburgh, Pa.
March 8, 1939.

Duly sworn to by Thomas Fitzgerald. Jurat omitted in printing.

[fol. 25]

SCHEDULE "B" TO PETITION

Liens

Filed by the United States against Pittsburgh Railways Company, debtor, certain of its underlying companies and Pittsburgh Motor Coach Company, subsidiary.

Pittsburgh Railways Company—

Income Tax Lien No. 3528 assessed 6/29/38 for years 1930-31-32 in amount of \$5,771,066.22; filed 7/19/38.

The Duquesne Traction Company & Affiliated Corp.—

Income Tax Lien No. 3565 assessed 7/14/38 for year 1937 in amount of \$1,251.40; filed 8/4/38.

Federal Street and Pleasant Valley Passenger Railway Company—

Income Tax Lien No. 3564 assessed 7/14/38 for the year 1937 in amount of \$3,451.20; filed 8/4/38.

Monongahela Street Railway Company—

Income Tax Lien No. 3567 assessed 7/14/38 for year 1937 in amount of \$40,624.39; filed 8/4/38.

Pittsburgh and Birmingham Traction Company—

Income Tax Lien No. 3568 assessed 7/14/38 for year 1937 in amount of \$18,852.05; filed 8/4/38.

Pittsburgh Incline Plane Company—

Income Tax Lien No. 3563 assessed 7/14/38 for year 1937 in amount of \$1,383.71; filed 8/4/38.

[fol. 26] The Suburban Rapid Transit Street Railway Company—

Income Tax Lien No. 3569 assessed 7/14/38 for year 1937 in amount of \$6,405.00; filed 8/4/38.

Pittsburgh Motor Coach Company—

Income Tax Lien No. 3529 assessed 6/29/38 for years 1930-31-32 in amount of \$5,771,066.22; filed 7/19/38.

IN UNITED STATES DISTRICT COURT

ORDER OF REFERENCE

And now, to-wit, March 10, 1939, the foregoing petition of W. D. George, Thomas M. Benner and Thomas Fitzgerald, Trustees of Pittsburgh Railways Company, debtor, and of Pittsburgh Motor Coach Company, subsidiary, having been presented in open Court, upon consideration thereof and on motion of Blaxter, O'Neill & Houston, counsel for petitioners, it is ordered, adjudged and decreed that said petition be and it is hereby referred to Watson B. Adair, Special Master, for a hearing and report thereon; that said hearing be held by the said Special Master on March 28, 1939 at 10:30 o'clock A. M., at Court Room No. 6, Sixth Floor, Federal Building, Grant Street, corner Seventh Avenue, Pittsburgh, Pennsylvania; that ten days' notice of the time and place of such hearing be given by mail to Pittsburgh Railways Company, debtor, and Pittsburgh Motor Coach Company, subsidiary, their creditors, claimants, stockholders and indenture trustees, their subsidiaries and affiliated companies and indenture trustees under their issues, the Securities and Exchange Commission, the Secretary of the Treasury, and all other persons interested in the within reorganization proceeding whose names appear on the books and records of the debtor and its subsidiary; [fol. 27] that a hearing on the petition and report of the Special Master, and on any exceptions filed thereto, be held by a Judge of this Court on the fifth day following the date of filing said report, excluding the date on which it is filed; and that notice of such hearing by a Judge shall be included in the notice to be given of the hearing before the Special Master.

By the Court, V.

[fol. 28] IN THE UNITED STATES DISTRICT COURT

OBJECTIONS OF THE TORT CREDITORS COMMITTEE TO PAYMENT
OF TAXES OR TAX ITEMS SET FORTH IN THE PETITION OF
THE TRUSTEES FILED MARCH 10, 1939—Filed April 14, 1939

To the Honorable, the Judges of said Court:

The Tort Creditors Committee at the hearing held the 28th day of March, 1938, before the Special Master, re-

serving the right to interpose further and additional objections, formally objected by notation on the record to the payment by the trustees of the several taxes due from the underlying companies in the Pittsburgh Railway System, for the following reasons:

1. That the taxes are the taxes of the underliers and not of the Pittsburgh Railway Company. That if the Railways is liable for such taxes it is because of a contractual obligation to the underliers and not by reason of any direct liability as a taxpayer to the United States Government or the Commonwealth of Pennsylvania therefor.

2. That no order authorizing the payment of taxes due from the underliers should be made unless and until the underliers are made parties to the proceeding. An application has been made to the Court to bring a number of the underliers into the proceeding and until this application is disposed of, nothing should be done relative to the payment of these taxes by the Pittsburgh Railways System. [fol. 29] The said Committee, by its undersigned counsel, further object to the payment of the taxes or tax items set forth in the prayer of the aforesaid petition for the following additional reasons:

3. It does not appear that there is any emergency or other immediate necessity for the payment of the tax items or tax claims due from the underliers in advance of the usual and ordinary times of payment in the reorganization proceeding—that is to say, at the time of or after the confirmation of the plan.

4. There is nothing in the petition to show particular or legal justification for the payment, at this time, of any of the tax items of the underliers.

A. E. Kountz, Lewis M. Alpern, Attorneys for Tort-Creditors Committee and Attorneys of Record for Various Creditors.

[fols. 30-31] IN UNITED STATES DISTRICT COURT

**Excerpts from Transcript of Testimony Taken at Hearings
Before the Special Master**

(Transcript filed August 22, 1939)

Hearing March 28, 1939, before Watson B. Adair, as Special Master, on Petition of Trustees filed March 10, 1939, Respecting Taxes

APPEARANCES:

For the Trustees: Blaxter, O'Neill & Houston, Esqs.,
by Messrs. Houston and O'Neill.

For Citizens Traction Company: Lee C. Beatty, Esq.

For Tort Creditors' Committee: Lewis M. Alpern, Esq.

For Allegheny Traction Company, Millvale, Etna &
Sharpsburg St. Ry. Co.: Hill Burgwin, Esq.

[fol. 32] **OBJECTIONS TO TORT CREDITORS' COMMITTEE**

MR. ALPERN:

The Tort Creditors' Committee, reserving the right to interpose further and additional objections, objects to the payment by the Trustees of the several taxes due from underlying companies of the Pittsburgh Railways System, for the following reasons:

First: That the taxes are the taxes of the underliers and not of the Pittsburgh Railways Company; that if the Railways Company is liable for such taxes, it is because of contractual obligation to the underliers, not by reason of any direct liability as a taxpayer to the United States Government or to the Commonwealth of Pennsylvania.

Second: That no order authorizing the payment of taxes due from the underliers should be made unless and until the underliers are made parties to the proceeding. An application has been made to the Court to bring a number of the underliers into the proceeding, and until this application has been disposed of nothing should be done relative to the payment of these taxes by the Pittsburgh Railways System.

Adjournment to April 14, 1939.

[fol. 33] Hearing April 14, 1939, before Watson B. Adair, Special Master, Pursuant to Adjournment from March 28, 1939, on Trustees' Petition for Instructions with Respect to Certain Taxes

Present:

For Trustees: Blaxter, O'Neill & Houston, Esqs., by Mr. O'Neill.

For Citizens Traction Company: Lee C. Beatty, Esq.

For Philadelphia Company: W. W. Booth, Esq., and W. A. Seifert, Esq.

For Allegheny Traction Company: Hill Burgwin, Esq.

For Tort Creditors' Committee: Lewis M. Alpern, Esq. and A. E. Kountz, Esq.

For Bureau of Internal Revenue: John D. Ray, Esq. and John E. Shea, Esq.

For City of Pittsburgh: R. B. Tucker, Jr., Esq.

Mr. Thomas Fitzgerald, one of the Trustees appeared, the other two trustees not being present.

* * * * *

C. T. HARMON, a witness called on behalf of the Trustees, being duly sworn, testified as follows:

Direct examination.

By Mr. O'Neill:

Q. Mr. Harmon, you are employed by the Trustees of the Pittsburgh Railways Company?

[fol. 34] A. Yes, sir.

Q. In what capacity are you employed?

A. Chief Accountant of the Statistical Division.

Mr. O'Neill: I wish to state to the Master that instructions were requested with respect to what should be done as to the payment of unpaid balances of Federal Income Taxes for the calendar year 1937, and the same taxes of certain underliers for the calendar year 1937, this appearing as Items (j) and (k) on pages 12 and 13 of the petition. However, the amount of the balances of these taxes are not stated and that I would like to get on the record.

(A paper marked as Trustees' Exhibit No. 1)

Mr. O'Neill:

Q. Mr. Harmon, there is no unpaid balance of Federal Income Tax for the Pittsburgh Railways Company for the year 1937?

A. That is correct.

Q. However, there is a balance owing on account of those taxes by certain underliers for those years?

A. That is right.

Q. At my request did you prepare a schedule of the amount of those taxes?

A. That is right.

Q. I show you a paper marked "Trustees' Ex. No. 1" and ask you if there is shown in that in the first column the unpaid balances of the Federal Income Tax for the calendar year 1937 of the underlying companies?

A. That is correct. The payments were due June 15, September 15 and December 15, 1938.

[fol. 35] The Master: Do I understand that this exhibit refers to paragraph (k) of the petition?

Mr. O'Neill: Paragraphs (j) and (k). Another tax we would like to have considered in connection with this application is the State Corporate Net Income Tax for the calendar year 1937. Mr. Seifert's comments so far as that state income tax is concerned were directed to the year 1938. No mention has been made in the petition of that tax for the calendar year 1937.

Q. Mr. Harmon, there is no balance of state corporate income tax due for the year 1937 by the Pittsburgh Railways Company?

A. No, there is no tax liability for Pittsburgh Railways Company.

Q. Did you at my request prepare a schedule of the unpaid state corporate net income tax due by the underlying companies for the year 1937?

A. Yes, sir.

Q. That tax for the year 1937 is payable when and how?

A. It is payable in semi-annual installments, April 15 and September 15, 1938.

Q. Of the year 1938?

A. 1938.

Q. Has the April 15, 1938 installment been paid?

A. It has been paid.

Q. I show you again the paper marked Trustees' Exhibit No. 1, and ask you if in the second column is shown the unpaid installment of the 1937 state corporate net income taxes due by the underliers in the year 1938?

A. That is correct.

[fol. 36] Q. In other words, the next installment would be payable May 15, 1938?

A. That is correct.

Mr. O'Neill: I offer in evidence Trustees' Exhibit No. 1.
The Master: Mr. Seifert, are the 1937 taxes subject to the same objections as the 1938 taxes?

Mr. Seifert: Precisely so, yes, sir.

E. C. DONAGHY, a witness called on behalf of the Trustees, being duly sworn, testified as follows:

Direct examination.

By Mr. O'Neill:

Q. Mr. Donaghy, you are employed by the Trustees of Pittsburgh Railways Company?

A. I am.

Q. In what capacity, Mr. Donaghy?

A. As chief of the Bond Records Division.

Q. Two other taxes we would like to have considered in connection with this petition of the Trustees are the federal income taxes withheld for the years 1937 and 1938, those taxes arising in connection with the covenants in bond issues whereby the obligor agrees to pay 2% of the income tax of the obligee on account of the income from those bonds?

A. Correct.

(A paper marked for identification as Trustees' Exhibit 2.)

[fol. 37] Q. Mr. Donaghy, you have prepared at my request a schedule of the taxes withheld or paid at source by Pittsburgh Railways Company and the underlying companies in connection with their bonds issued for the year 1937?

A. I did.

Q. I show you a paper marked Trustees' Exhibit No. 2, and ask you if that schedule appears in the first column shown on that exhibit?

A. That is correct.

The Master: Schedule of what?

Mr. O'Neill: Schedule of the amount of taxes in connection with interest paid on tax free covenant bonds of the Debtor and underlying companies during the year 1937.

The Master:

Q. What is your answer, Mr. Donaghy?

A. That is correct, yes, sir.

Mr. O'Neill: This is just for 1937. He is speaking of the first column.

The Master:

Q. As I understand, the first column indicates the tax which the Pittsburgh Railways Company or the respective underlier assumed and agreed to pay with respect to interest which was paid during the year 1937, is that right?

A. Yes, sir.

Mr. O'Neill:

Q. Does this exhibit, in the second column show the same situation with respect to the year 1938?

A. It does, sir.

[fol. 38] Q. The tax shown for the year 1937, \$9,832.53; is payable when?

A. June 15, 1938.

Q. And the tax shown for the year 1938, \$4,203.75, is payable when?

A. It will become due on June 15, 1939.

The Master:

Q. Are these amounts based on interest which was actually paid, or merely interest or partly interest which was deposited with disbursing agencies, whether it was paid out or not?

A. Those would represent only those items where the interest was actually paid.

Mr. O'Neill: We offer in evidence Exhibit No. 2.

Q. Mr. Donaghy, you are familiar with the state corporate loan taxes of the Debtor and the underliers, is that correct?

A. Yes, sir.

Q. The reports due by the underliers are filed by the underliers, is that correct?

A. That is correct.

Q. And the settlement for the tax by the Department of Revenue is made against the underlier in each particular case, is that correct?

A. That is correct.

Q. But remittance for the tax has been made by Pittsburgh Railways Company by its check, is that correct?

A. That is correct.

Q. The Pittsburgh Railways Company paid the interest which produced the corporate loan tax, at least prior to May 10, 1938, the time the reorganization proceeding began?

[fol. 39] A. It was deposited on their check, yes, sir.

Q. Do I understand you to say that amounts to cover the interest deposits were deposited by Pittsburgh Railways Company by its own check?

A. Yes, sir.

Q. And that was the money used to pay the installments?

A. Yes, sir.

The Master:

Q. Where was that deposited?

A. With paying agencies.

Q. What amounts with reference to the amount of interest due, did the Pittsburgh Railways Company deposit? That is, did it deposit the face amount of the interest due?

A. It deposited the face amount of the interest which was due.

Q. Do you know whether all the bonds contained provisions that the obligor was to pay the interest without deduction for state tax, or did it vary?

A. They varied. Their mortgage would vary.

Q. Where the debtor would not agree to pay for redemption, did the Pittsburgh Railways Company still deposit the face amount of the interest?

A. Yes, sir.

Q. Then when the deposit was made, what became of the amount returned?

A. That was returned to the Pittsburgh Railways Company by the paying agents.

Q. Were those returns to the Pittsburgh Railways Company made before May 10, 1938?

A. Yes, sir.

Q. All of them?

A. The return of the state corporate loan deducted by the paying agent, that was returned before May 10. How- [fol. 40] ever, there is an item involved in the Pittsburgh Railways Company where it was not, having been deducted from interest deposited by the Trustees.

Q. Do you know how much that is?

A. No, sir. I believe it is included in Mr. O'Neill's petition. I don't recall the specific amount of it.

Mr. O'Neill:

Q. You are referring to amounts actually withheld?

A. Yes, sir.

Q. That shows in the petition prior to May 10, 1938 and after, in connection with Car Trust Certificates, is that correct?

A. That is correct.

Mr. O'Neill: That appears on page 4, paragraph 12.

I now offer in evidence the petition filed by the Trustees which has been the subject of this hearing:

HEARING ON TRUSTEES' PETITION WITH RESPECT TO CERTAIN
TAXES, RESUMED JUNE 9, 1939, PURSUANT TO ADJOURN-
MENT FROM MAY 25, 1939

Present:

For Trustees: J. Henry O'Neill, Esq., of Blaxter, O'Neill & Houston, Esqs.; Messrs. George and Fitzgerald, Trustees.

For Citizens Traction Company: Richard W. Ahlers, Esq.

For Philadelphia Company: W. A. Seifert, Esq.
[fol. 41] For City of Pittsburgh: R. B. Tucker, Esq.

For Securities and Exchange Commission: Marland Gale, Esq.

For Committee for Municipalities' Interests: Walter M. Newman, Esq.

D. C. DONAGHY, a witness called on behalf of the Trustees, being duly sworn, testified as follows:

Direct examination.

By Mr. O'Neill:

Q. Mr. Donaghy, you are employed by the Trustees of the Pittsburgh Railways Company?

A. I am.

Q. In what capacity?

A. As Chief of the Bond Tax Bureau.

Q. And you were employed by the Philadelphia Company and its affiliated companies prior to the time of your employment by the Trustees?

A. That is correct.

Q. And I imagine you are still employed by the Philadelphia Company and its affiliated companies, besides the Pittsburgh Railways Company and Pittsburgh Motor Coach Company?

A. That is right.

Q. Are you familiar with the method and manner of paying the Pennsylvania corporate loans tax that was in effect prior to May 10, 1938?

A. I am.

Q. Will you state what the mechanical steps were in [fol. 42] connection with that tax? In other words, how was the interest paid?

A. Deposited or paid. Deposited by a voucher drawn by the Pittsburgh Railways Company, in the event of underlying companies, with the paying agent. The instructions regarding deductions for corporate loan tax were that any such taxes were to be deducted from the holders.

Q. And such a tax would be deducted from the holders if there was a limit on the obligation of the issuer of the bonds?

A. That is correct.

Q. You say the paying agents in cases where a deduction was to be made. You withheld that amount of taxes from the bondholders?

A. From the taxable bondholders.

Q. Then what would become of that money?

A. That money at the close of the month would be returned to the company marked "Pennsylvania Tax deducted from taxable residents of the state."

Q. Do you mean deducted by the paying agent?

A. That is correct.

The Master:

Q. You say it was returned at the end of the month. What month?

A. At the end of the month in which the coupon to be taxed matured. It is customary for the paying agent to make a monthly return.

Q. Would they withhold the money until all the coupons were in?

A. No, sir. They would hold it until the close of the month. It is not usual for all the coupons to be presented in the same month in which they mature.

Q. Then they returned the tax deductions which were made that month?

[fol. 43] A. Yes, sir.

Q. But the balance of the money available for the interest is held by the paying agent?

A. Until the payment is made, yes, sir.

Mr. O'Neill:

Q. With respect to the corporate loans tax for the year 1938, can you tell us how much tax was withheld from bondholders on account of interest that was paid by the Pittsburgh Railways Company prior to May 10, 1938?

A. About \$302.00.

Q. Now, the practice you have described is the same after May 10, 1938, with respect to interest paid by the Trustees on car trust bonds?

A. That is correct.

Q. What amount of interest in that instance, if any, was actually withheld from the bondholders and marked by the paying agents—marked as described?

A. \$182.00.

Q. Now, Mr. Donaghy, you are not familiar with what happened to the checks after they came back to the organization, or to the Trustees?

A. No, sir. That is a Treasurer's Office function.

The Master:

Q. Do the deductions amounting to \$302.00 represent deductions from interest owing by the Pittsburgh Railways Company on its own obligations or on interest owing by underlying companies on their obligations?

A. The answer would be that there are two companies involved in that \$302, the Central Passenger Railway Company with an amount, I believe of \$34.20, and the balance is a deduction from the car trust bonds to the Pittsburgh Railways Company. In respect to that \$34.20, that \$34.20 represents the amount of tax owing on Central Passenger Railway bonds, after a deduction has been made for the [fol. 44] Treasurer's commission allowed by the State for making collection, but the total amount of tax deducted would have been \$36 and would have been so associated in the \$302.

Mr. O'Neill:

Q. Mr. Donaghy, turning from state corporate loan tax to federal tax withheld—in other words, income tax withheld at source. Will you explain how that works? As I understand it, no money is actually withheld from bondholders?

A. That is correct. That is a misnomer in there in regard to the taxpayer's taxable status. It represents an indication by the bondholder that he wishes to avail himself of the 2% tax covenant in the mortgage and he so indicates when he prepares the ownership certificate, which he presents with his coupon. That indication is not known to the Company until the certificate of ownership reaches us. After it reaches us it is then included in the monthly return to the Commissioner of Internal Revenue, in which we set forth the name, the address of the owner and the amount of interest he has received and calculate a 2% tax on it. That tax is then accumulated for the entire record for that particular month. At the close of the year we summarize our monthly returns, setting forth in the summarized report only the amount of taxes for each respective month.

That summarized report must be filed on or before March 15 of the year following that for which the returns were filed and we are assessed on the 15th day of June.

Q. Mr. Donaghy, I show you a paper which was offered in evidence as Exhibit No. 2 at the hearing on this tax petition held April 14th, 1939. It is shown on that exhibit that you mean the tax withheld at source for the year 1937 is in the amount of \$9,832.53, is that correct?

A. That is correct.

[fol. 45] Q. And that the same tax for the year 1938 is in the amount of \$4,203.75?

A. That is correct.

The Master:

Q. That is 1938 paid to when?

A. The entire year for 1938, for which the tax will come due on the 15th of this month.

Q. Were any payments made in 1938 after May 10th?

Mr. O'Neil: The Trustees made payments on the car trust bonds and I believe the Philadelphia Company made payments on its guarantees.

The Witness: That includes payments prior to the trusteeship by the Debtor Company and those car trust securities on which the Trustees paid interest after they went in office.

Mr. O'Neill:

Q. And of the amount of \$4,203.75, the \$110.40 represents the tax payable at source on interest paid by the Trustees on the car trust bonds?

A. That is correct.

The Master: Q. What does the rest represent?

Mr. O'Neil: It shows the issues on which they were paid, on the exhibit.

The Master:

Q. Can you tell, Mr. Donaghy, how much of this \$4,203.75 is derived from interest paid prior to May 10, 1938?
[fol. 46] A. All of it would be, except this \$110.40 referred to in Item "C". That would be approximately \$4100.

H. D. MEGAHAN, a witness called on behalf of the Trustees, being duly sworn, testified as follows:

Direct Examination.

By Mr. O'Neill:

Q. Mr. Megahan, you are employed by the Trustees of the Pittsburgh Railways Company?

A. I am.

Q. In what capacity?

A. I am Assistant Treasurer, for them.

Q. And you are also employed in the same capacity by the Philadelphia Company and its affiliated companies?

A. I am Assistant Treasurer for the Philadelphia Company and all its subsidiaries.

Q. And I believe you were so employed prior to this reorganization proceeding?

A. I was.

Q. You are familiar with the bank accounts then of the Debtor before May 10, 1938, and of the Trustees subsequent to June 14, 1938?

A. I am.

Q. And you are also familiar, I believe, with the handling of the checks that would be returned from paying agents in connection with corporate loan tax withheld from bondholders?

A. Right.

Q. You heard Mr. Donaghy's testimony with respect to return of those checks?

A. I did.

[fol. 47] Q. When a check would be received by Pittsburgh Railways Company prior to May 10, 1938, covering this remittance of tax from the paying agent, do you know where that check would be deposited?

A. In the Farmers Deposit National Bank, as a general rule.

Q. In what account, a special account, or a general account?

A. In a general account.

Q. Did the Company have a separate account for corporate loan taxes?

A. As far as I know the Company has never carried a special account for tax purposes.

Q. In other words then, the check would be deposited in the general account of the Pittsburgh Railways Company?

A. That is correct.

Q. Mr. Donaghy testified that the amount of tax remitted by paying agents to the Railways Company for the year 1938, the corporate loan tax, was in the amount of about \$302. Do you know whether the general account of Pittsburgh Railways Company at the Farmers Deposit National Bank on May 10, 1938, was in excess of \$302?

A. Considerably in excess of that amount.

The Master:

Q. Was that account continuously in excess of that amount from the first of January, 1938—in excess of \$302—since the first of January, 1938?

A. Since that time and before that time, as far as I know, it has always been substantially in excess of that amount.

Q. Well, you do know?

A. Yes, sir.

[fol. 48] Mr. O'Neill:

Q. Mr. Donaghy testified that the amount of tax withheld from bondholders in connection with interest payments made by the Trustees and returned to them by the paying agents was \$182. Do you know in what account that check for those funds would have been deposited by the Trustees?

A. That would go in the same account in the Farmers Deposit National Bank.

Q. Do the Trustees have a special account for corporate loans taxes?

A. They do not.

Q. Can you state whether or not on June 14, 1938, the amount in that account in the Trustees' name was in excess of \$182?

A. Substantially in excess of that amount.

Q. And it has continued to be substantially in excess of that amount from June 14, 1938 to date?

A. It has.

Q. During the period from May 10, 1938 to June 14,

1938, or while the Debtor was in possession, did that debtor have a separate corporate loan tax account?

A. It did not.

Q. It did have a general account in the Farmers National Bank, is that correct?

A. That is correct.

Q. And was the balance in that account at all times during that period in excess of \$302?

A. It was.

The Master:

Q. I think you said that the remittances were generally put in that account.

A. They were generally put in that account. The Farmers Deposit National Bank is not the only bank, but that [fol. 49] is the main depository for the Company funds of the Trustees.

Q. Was that the account on the first of January, 1938, in which the tax remittances from the paying agents were actually deposited?

A. That is correct.

Mr. O'Neill:

Q. Did either the Pittsburgh Railways Company before May 10, 1938, or the Debtor after May 10, 1938 and before June 14, 1938, or the Trustees subsequent to June 14, 1938, ever have a separate tax account in connection with taxes withheld at source?

A. They have not.

Q. And whenever that tax had been paid by Pittsburgh Railways Company, the funds were drawn on what account?

A. On the account in the Farmers Deposit National Bank always.

Q. The general account?

A. Yes.

The Master:

Q. Were the moneys which were transferred to paying agents for the purpose of paying interest always drawn from any one account?

A. That same account.

Q. Was there always left in that account after transferring funds to the paying agents more than enough to cover this constructive retention of tax?

A. There was.

Q. And did the bank balance always exceed the total of those constructive retentions, plus the tax remittances from the paying agents?

A. It did.

Q. Was all interest paid through paying agents?

[fol. 50] A. Yes, sir.

Mr. O'Neill:

Q. Was the general account in the Farmers Deposit National Bank of Pittsburgh Railways Company, prior to May 10, 1938, and of the Debtor during the period from May 10, 1938 to June 14, 1938, and of the Trustees subsequent to June 14, 1938, always substantially in excess of the sum of \$14,000; being the approximate total amount of the Federal tax withheld at source for the years 1937 and 1938?

A. It was.

Q. That is, plus the sum of \$484, being the total amount of corporate loans tax deducted from interest paid to bondholders during the year 1938.

A. The answer is still the same—that it was.

Cross-examination.

By Mr. Kountz:

Q. Mr. Megahan, in addition to this money you spoke of, are there any other trust funds of other people in that account, as far as you know, or were there during the period Mr. O'Neill referred to?

A. That is more or of a legal question as to what constitutes trust funds.

Q. What I have in mind is,—there might be a presumption that this money belongs to these taxing authorities, but that there are other possible trust funds in the same account?

A. Trust funds as such, strictly speaking, there were no trust funds in that account. As far as we treated it that was a general account of the Company used for all purposes.

Q. You do not have any reason now to suppose that [fol. 51] anybody else would come in here and claim any of these funds as trust funds, is that correct?

A. I would hesitate to say, because I don't know—

Mr. Seibert: Objected to.

Mr. Kountz: Your Honor, all we are concerned with is whether somebody else might come in here and claim a part of this fund.

The Master:

Q. Do you know of any other possible claims that might be made against this fund as trust funds of any nature?

A. It would depend, of course, on how you treated wages due employees. I don't know how that is treated. That would be a legal question.

Q. It might apply to Social Security taxes retained?

A. If that would be true then it would be in that fund.

Q. In addition to those other taxes?

A. That is correct.

Mr. O'Neill:

Q. Mr. Megahan, will you explain how the sharing of Social Security taxes owed by the employees of the Company is handled in the bank accounts?

A. So far as the bank accounts are concerned, and the payroll accounts, there are special accounts set up periodically called "Paymasters Accounts". In those accounts are deposited just sufficient funds to meet the payroll of that particular period, with the deduction having been made prior to the time the money was deposited in the payroll accounts for any tax due.

Q. In other words, the tax deducted remains in the general account.

[fol. 52] A. That is correct.

Q. And that was the practice of the Railways Company prior to May 10, 1938, and of the Debtor in possession, and is the practice of the Trustees?

A. Yes.

Q. And was the balance in the general account, at the Farmers Deposit National Bank, of the Pittsburgh Railways Company, prior to May 10, 1938 and of the Debtor while it was in possession between May 10, 1938 and June 14, 1938, and of the Trustees subsequent to June 14, 1938,

always substantially in excess of the total amount of the following taxes that were discussed here this morning: Pennsylvania Corporate Loans Tax withheld from interest paid to resident bondholders; Federal Income tax withheld at source for the years 1937 and 1938, and the employees' share of the Federal Old Age Compensation tax?

A. Without knowing the amount of the Federal Old Age Compensation tax, I could not answer that definitely. I could answer it in a general way, by saying that the amount in the general account at the Farmers Deposit National Bank since May 10, 1938, has never been less than \$75,000.

Q. And before May 10, 1938?

A. How far before?

Q. Well, at any time during the period from January 1, 1938 to May 10, 1938?

A. On January 3, 1938, the balance in the Farmers Deposit National Bank was \$245,000. On May 10, 1938, the balance in the Farmers Deposit National Bank was \$108,000, and on June 14, 1938, the balance in the Farmers Deposit National Bank in the general account was approximately \$601,000.

The Master:

Q. Well, that doesn't tell us the low points: From Jan- [fol. 53] uary 1, to May 10, 1938, what was the low point of your deposit?

A. February 28.

Q. How much was it then?

A. \$51,000 in the Farmers Bank and total in all depositories of \$91,000.

Q. From May 10, 1938 to June 14, 1938, what was your low point in this general account?

A. In the Farmers Bank, without knowing definitely, I would say that May 10th itself was the low point, because at June 14th the account had grown to \$601,000.

Q. And after June 14th, 1938?

A. Since June 14, 1938, I think I can safely say it has never dropped below \$500,000. I could get you the exact figure and the low date.

Mr. O'Neill:

Q. Mr. Megahan, you are familiar with the amount of the monthly payroll of the Trustees?

A. The approximate amount, yes.

Q. And also the payroll of the Pittsburgh Railways Company before the trusteeship?

A. Yes.

Q. Based on that, are you able to make an estimate of what you think the employees' share of the Federal Old Age Compensation tax would run per month?

A. The payroll of the Pittsburgh Railways Company for sometime has run, I would say, as an estimated payroll, between \$450,000 and \$520,000 per month.

The Mast :

Q. Is that true ever since the first of April, 1938?

A. Yes.

Q. Then the Social Security tax of 1% would not exceed \$5300 during a month?

A. That is true. And there was always that amount of [fol. 54] money in the general accounts at the Farmers Deposit National Bank and sufficient to cover any other taxes we have discussed in this proceeding.

THOMAS FITZGERALD, a witness called by Counsel for the Trustees, being duly sworn, testified as follows:

Direct Examination

By Mr. O'Neill:

Q. Mr. Fitzgerald, you are one of the Trustees of the Pittsburgh Railways Company?

A. Yes, sir.

Q. Mr. Fitzgerald, would it be possible to determine the net earnings of the separate underlying companies of the Pittsburgh Railways System, over the period the Company has been in the reorganization proceeding, in other words, from May 10, 1938 to date?

A. No, sir.

Q. Would you state why it would not be possible to do so?

A. I prepared a statement which I would like to read in answer to that question. Since the Pittsburgh Railways System was created in 1902, there has been absolutely no effort to account for revenues and operating expenses of individual underlying companies. The most rational approach to a method of doing so would require an origin and destination stated for each ride taken. An attempt to do

this would be tremendously expensive and would entail so many assumptions as to the allocation of proportions of fares that it could not be used as a dependable basis for allocating revenues to individual companies. To attempt [fol. 55] to apply estimates of operating expenses against any method of estimating earnings, would only accumulate additional assumptions and produce a net earnings estimate which would contain a multiplication of errors and therefore have no meaning. The only way in which the net earnings of each underlier could be determined would be to operate each independently. This would be of no value in our present problems and would be physically and commercially impossible. It would not be satisfactory to the public, or to the municipal and state authorities.

Cross-examination.

By Mr. Seifert:

Q. Mr. Fitzgerald, did you say the Pittsburgh Railways System had been operating as a unified system since 1902?

A. That is my understanding.

Q. Practically all of the underliers were operating back of that period?

A. I would say substantially all of them, yes, sir.

Mr. Alpern:

Q. Mr. Fitzgerald, do you know at the present time whether the Trustees are in a position to advise the Court which properties of the underliers, or the property of which underliers, it is the intention of those responsible for the reorganization of the Company to reject?

Mr. O'Neill:

Mr. Fitzgerald is not one of the Reorganization Trustees. Mr. George and Mr. Benner, the other two Trustees of the Pittsburgh Railways Company, are the ones directed to prepare and file the Plan of Reorganization. In fact, they both are in Court this morning and we intend to put Mr. [fol. 56] George on the stand to say what he can say about the future use of the properties of the underliers.

Mr. Alpern:

I have understood all the time that Mr. Fitzgerald is the operating head of the System and is familiar, no doubt with

the value of the properties, and whether or not certain properties have no value.

Mr. O'Neill:

But Mr. Fitzgerald has no duties whatsoever under the court order and anything Mr. Fitzgerald would say would in a sense be hearsay, compared to what Mr. George would say. I don't object to your question—I want to advise you and also the Master, that the Trustee to whom I think your question should be directed will be put on the stand and will be glad, I know, to answer your question. I merely point out that you are asking your question of the Trustee who has no authority as to what will be done with the Plan.

Mr. Alpern:

Q. Mr. Fitzgerald, you are operation head of the Pittsburgh Railways System?

A. Yes, sir.

Q. And you have been engaged in the operation of the system for how long?

A. Since 1924—as active head of the organization.

Q. And also since the filing of this court proceeding?

A. Yes, sir.

Q. Now, I would like to renew my question.

A. My answer to the question is, No, I do not know.

Mr. Seifert:

Q. Mr. Fitzgerald, have the Trustees either affirmed or disaffirmed any of the leases under which the Pittsburgh [fol. 57] Railways Company operate and did operate prior to the appointment of yourself and two associates as Trustees under 77-B?

A. They have neither affirmed or disaffirmed.

The Master:

Q. Mr. Fitzgerald, do you know any way other than ascertainment of earnings for the determination of fair rental value of the properties of the underlying companies which have been utilized by the Pittsburgh Railways Company or its Trustees since May 10, 1938?

A. I think that question should be answered by the Reorganization Trustees. I at present know of no method of

determining what relative rentals should be paid to the various underlying companies.

Q. You are not prepared then to give any evidence on that question?

A. No, sir. I would have to make a more intensive study of that particular problem than has been made heretofore before I could answer it. At the present time there are not available sufficient net earnings to make that a question.

The Master:

Well, the question is likely to confront the Court in the proceeding.

Mr. Alpern:

Q. Mr. Fitzgerald, since your appointment as one of the Trustees of the Pittsburgh Railways Company in this present proceeding, have you yourself given any thought to, or have you any views with respect to which properties of the Railways Company, or of its leases, should be rejected, and which should be taken up by the Trustees?

A. Inasmuch as we are not making any payments on any of the securities of the underlier companies—the only pay-[fol. 58] ments we are making are on the car trust bonds—the question of the abandonment of these properties would not be immediate. Now, there has been some consideration given to the abandonment of some properties, such as some of the inclines; the possibility was considered of abandoning the interurbans, but in the case of the interurbans if we had abandoned them—say last May—our estimate is we would now be \$50,000 worse off at the end of the year than we were, so the thought is that the interurbans bring in more than the actual cost of maintaining the service, and it would be a mistake to abandon them. However, if large expenditures are necessary on the interurbans, I think the thought then will be to abandon them. We have to secure the permission of the Public Utilities Commission before any abandonment can be made effective.

Mr. Alpern:

Q. And the Trustees have not yet come to a decision on the question of abandonment of this property, or any property?

A. No, that is a very difficult question to arrive at, because we do not know what the effect of abandonment will be, or just what the effect of the abandonment of any par-

ticular property would be. Even the question of the incline is pretty hard to determine.

Q. Many of these leases between the Railways Company and the underliers have forfeiture clauses have they not?

A. Do you mean cancellation clauses?

Q. Yes, sir.

A. There are some terminations in them, but generally the operating agreements have cancellation clauses in them.

Q. And the franchises granted to the Pittsburgh Railways Company or to the underliers have provision for continuous operation of the underliers or their assignors, do you know that?

[fol. 59] A. That has generally been the term of the franchises I have been acquainted with in the past.—I don't know.

Q. If there is a breakup and the right of forfeiture was exercised by the assignors, could any of these underliers afford to operate their system independently?

A. I think that it would be a very difficult if not impossible proposition for any of the underliers to operate the property over which their securities extend.

Mr. Kountz:

Q. Mr. Fitzgerald, is it not a fact that most of those franchises of the underliers contain provisions permitting the forfeiture of the franchises if the line is not in operation?

A. I don't know whether it has permission to forfeit, or whether it is mandatory, but as a matter of fact, the forfeiture of a franchise through non-use would not affect the operation particularly, in my opinion, because if the rest of the property covered by the franchise is used by and useful to the public, service there would hardly be interrupted. Franchises have a theoretical value but it is largely theoretical.

W. D. GEORGE, a witness called by Counsel for the Trustees, being duly sworn, testified as follows:

Direct examination.

By Mr. O'Neill:

Q. Mr. George, you are one of the Trustees of the Pittsburgh Railways Company?

A. I am.

Q. And I believe you and a co-trustee, Mr. Benner, are the Trustees who are directed by the Court to prepare and [fol. 60] file a Plan of Reorganization for Pittsburgh Railways Company?

A. That is correct.

Q. Mr. George, will you state whether the Trustees are now using and operating the properties of the various underlying companies whose taxes have been discussed here this morning?

A. That is correct.

Q. As one of the two Trustees charged with the duty of preparing a plan, would you be in a position to make a statement with respect to what possible use may be contemplated for the property of these underliers under the Plan of Reorganization you have in mind?

A. In a general way, I believe that the properties will be operated as they are now laid out. That is, I do not believe there will be a great amount of abandonment of any part in the reorganization. I think most of the properties which are now in use will continue in use.

Q. A provision for the use of those properties would, in all likelihood, although you cannot say definitely, be made in the Plan of Reorganization?

A. I believe that is true.

Mr. Kountz: I would like the record to show, instead of the motion to strike it out, that our position is that the answer is of little value here, because it assumes a number of things. It assumes that the underliers' properties will be taken over and the taxes paid, whereas, as I pointed out before, the final result might be a divestiture of taxes, and we feel the answer is too general to be the basis of any finding here.

Mr. Seifert: I would say in the present situation Mr. [fol. 61] George has answered that sufficiently. What eventually they may do is something for the Court later. Up to the present time the Trustees have taken no steps to abandon any of these leases. I think Mr. Kountz' objection is without any merit and I so submit to Your Honor.

The Master: It is manifestly impossible at this stage of this proceeding to determine what properties will be retained and what properties will not be retained. The Trustees themselves cannot entirely control or determine the

answer to that question. The Trustees are here asking instructions with respect to paying taxes and it may be that the degree of probability that certain properties will continue to be operated by this Company, or a new company, would have some bearing upon the action that the Trustees could wisely take with regard to the taxes. If there were some properties whose retention was quite doubtful, the payment of taxes with respect to those properties might be less advisable than the payment of taxes on properties which were almost certain to be retained. Whether it is feasible at this time to determine any schedule of property to be retained I do not know.

Mr. Seifert:

Q. Mr. George, have you and your associate trustees reached any conclusion as yet as to which companies which are presently operated by you as Trustees under 77-B will be abandoned?

A. With regard to that, I would not care to go any further than the statement I have made.

Q. I believe the statement you have made, as I understand, is that you and your co-trustees regard substantially all the properties as they are presently operated as necessary for future operation of the reorganized company?

A. I would have to answer that as I did your other question.

The Master:

Q. In other words, the matter is too uncertain to give any opinion, is that it?

A. Too uncertain.

Mr. Seifeit:

Q. At any rate, Mr. George, the properties whose taxes you have asked to have considered by the Master as to payment of taxes, are presently being operated by the Trustees under 77-B?

A. Yes, sir.

Mr. W. D. GEORGE, recalled:

The Master:

Q. Mr. George, do you consider it practicable at this time for the Trustees to say what properties of the underlier companies will and what will not be embraced in the contemplated Plan of Reorganization?

A. I do not.

Adjournment to July 6, 1939, at 10:30 A. M.

[fol. 63] Hearing on Above Matter Resumed July 6, 1939, at 10:30 A. M. on Trustees' Petition with Reference to Payment of Taxes Pursuant to Adjournment

Present:

For the Trustees: J. Henry O'Neill, Esq.

For the City of Pittsburgh: Richard B. Tucker, Jr., Esq.

For Tort Creditors' Committee: Bernard Goodman, Esq.

For the Philadelphia Company: William A. Seifert, Esq.

For Citizens Traction Company: Richard W. Ahlers, Esq.

C. F. Ligo, being duly sworn, testified as follows:

Direct examination.

By Mr. O'Neill:

Q. Mr. Ligo, you are employed by the trustees of the Pittsburgh Railways Company in the capacity of Chief Analyst?

A. I am.

Q. Are you familiar with the budget and estimated income and expenses for the twelve months ending May 31, 1939 which the trustees filed in connection with their petition requesting leave to make renewals, replacements and improvements to the debtor's properties?

A. I am. It was prepared under my supervision.

Q. Mr. Ligo, did you at my request yesterday prepare

a breakdown of certain items which appear under the heading "Income Deductions" of that estate?
[fol. 64] A. I did.

(A paper marked as Exhibit Number 3.)

Q. Mr. Ligo, I show you a paper marked Trustees' Exhibit Number 3 and I ask you if that is the breakdown of the particular items I spoke to you about?

A. It is.

Q. Now, first as to the item headed "Rent" which appeared on the budget under "Income Deductions", \$2,418,859, would you state the principal items which are comprised within the word "rent"?

A. The amounts shown here comparatively are the actual amounts accrued on the books for this item of rent breakdown as follows: Interest on funded debt of leased property \$1,441,645, interest on unfunded debt of leased property \$137,396.00.

Rentals \$830,275.00 or a total of \$2,409,316, which compared with the \$2,418,859 included in the budget.

Q. In other words, the \$2,409,316 is the amount that was actually accrued for the budget period?

A. That is correct.

Q. Now, what is comprised within the "Interest on Funded Debt of Leased Property"?

A. That represents the interest on outstanding bond issues of leased companies.

Q. Do you mean the underlying companies?

A. I do.

Q. How many of these companies are there?

A. 33 companies.

Q. Can you state the number of bond issues that would be issued by those bond issues?

A. 42 bond issues.

Q. Of those companies, can you state which ones own tracks?

A. 27 of these 33 companies own tracks directly.

[fol. 65] Q. Now, as to the subdivision here as follows "Interest on Unfunded Debt of Leased Property". Will you state what items are comprised in that?

A. That is made up of interest on the demand notes of the Consolidated Traction Company and the United Traction Company held by the Philadelphia Company and the Duquesne Light Company.

Q. And the interest on those notes was payable by Pittsburgh Railways Company?

A. It was, yes sir.

Q. Now, will you tell us as to the last subdivision under the caption "Rentals" on this Exhibit 3. Will you state what that item is comprised of?

A. It represents the amount of rent provided for in the various agreements payable to the underlying companies.

Q. Do you mean those would be flat, fixed sums?

A. Flat, fixed sums, variable according to any reduction in stock that might be made by the Pittsburgh Railways Company purchasing those stocks. In other words, that varies with any reduction in the outstanding stock—that is in general.

Q. Do I understand that the rent was calculated to be in an amount that would be sufficient to pay a certain rate of dividends on stock of underlying companies?

A. That is correct.

Q. Mr. Ligo, can you state how many underlying companies received such rentals as you have described?

A. Fifteen.

Q. And certain of those 15 are included in the 27 companies?

A. That is correct. 11 of these companies which received rent also are included in the item above "Interest on Funded Debt of Leased Property".

[fol. 66] The Master:

Q. As I understand it, many of these lessor companies—so-called—were not the direct lessors of the Pittsburgh Railways Company, but underlay the United Traction Company or Consolidated Traction Company, is that correct?

A. That is correct.

Mr. O'Neill:

Q. I direct your attention to the item under "Income Deductions" which reads "Taxes of Lessor Companies" in the amount of \$184,874.00 and I ask you what that item consists of?

A. This item consists of Federal income tax and State corporation net income tax. The amounts carried on the books for the twelve months ending May 31, 1939 were as

follows: Federal Income Tax \$119,810.00, State Corporation Net Income Tax \$49,752.00, or a total of \$169,562.00, which compares with the budget amount of \$184,874.00.

Q. And the trustees have accrued the Federal income tax item by reason of the fact that they have accrued interest and rentals that would be payable to the underlying companies?

A. That is correct.

Q. And for the same reason, they have accrued the State Corporation net income tax?

A. That is correct.

Q. Now, will you look at the item on the page under "Income Deductions" which reads "Miscellaneous (including tax on bond interest) \$85,677.00" and tell us of what that consists?

A. It consists of the following, these amounts being the actual amounts accrued on the taxes.

Q. You are reading from Exhibit 3?

A. That is correct. Corporate Loan Tax \$44,750.00, Federal Tax on Bond Interest paid or refunded (income at source) on leased property \$3,850.00, Federal Tax on [fol. 67] income at source \$2,825.00, miscellaneous \$107.00, and Interest during construction a credit of \$4,990.00, or a total of \$46,542.00, which compares with \$85,677.00 on the budget.

Q. Will you explain the reason for the difference between the budget amount and the actual amount you have just stated?

A. For the period of June 1 to December 31, 1938, the full amount of corporate loan tax, that is on the same basis as prior to the trusteeship, was accrued. Beginning January 1 to May 31, 1939, only the corporate loan tax on car trust interest was accrued. I think the books will be adjusted in order to make the books sustain that. This is the only type of tax where they change over. I think probably \$30,000 will be added to that accrual for corporation loan taxes.

The Master:

Q. Does this corporate loan tax \$44,750 represent the tax in respect to corporate loans on which the interest was actually paid?

A. No. This does not represent any payments here; but there is one of interest that has been paid and that is inter-

est on car trust certificates. That represents about \$550 a month. Now, your total corporate loan tax prior to trusteeship represents \$6,000 a month or \$72,000 annually and to make it consistent with the way the income taxes are being accrued, I have it accrued on the old basis, even though it has not been paid, inasmuch as they are accruing the full interest. I think the budget amount or \$85,677 is closer to representing the picture than this \$46,000—it's half and half—7/12ths of one and 5/12ths of another,—that just come up in this thing yesterday.

Mr. O'Neill:

Q. The figures which appear in the last column on Exhibit 3 do not represent payments but only accruals made for the same period as the budget covered?

[fol. 68] A. Yes, sir.

Mr. O'Neill: Exhibit 3 is offered in evidence.

Mr. Tucker:

Q. I would like to know on what basis the accrual was made on the Federal income tax?

A. That was made on the basis that if the interest were paid this would be the income tax—all our income tax.

Q. Does that include rentals?

A. Yes, sir.

Q. And the figures stipulated in the leases?

A. On the figure that is accrued on the books. It may not be at the same rate as was on the original agreement because that may possibly be changed.

Q. It does not represent any use and occupation basis?

A. No, sir. This is the same as accrued prior to the trusteeship.

Mr. O'Neill:

Q. In fact, it carries forward the old basis?

A. Yes, sir.

Mr. Seifert:

Q. Do I understand as to that item of State Corporation Net Income Tax \$49,752, you make an accrual that the State corporation net income tax would apply to the companies whose properties are leased and no longer operated by the company which owns that property?

A. That is correct. That is the basis on which this is accrued, but I understand that a recent court decision eliminates this tax.

Q. But that recent court decision has not become effective?

A. I don't know.

Q. But there has been an adjudication by Judge Hargest in Dauphin County that the state corporate loan tax is [fol. 69] a tax on the privilege of doing business and as such it would not be applicable to this case.

A. That is my understanding.

Q. No appeal has been taken to the Supreme Court from the Dauphin County case?

A. Not as far as I know.

Mr. O'Neill:

Q. Mr. Ligo, would you be prepared to state whether the Pittsburgh Railway Company has accrued on its books charges against United Traction Company, Consolidated Traction Company and certain underlying companies with respect to extraordinary repair or additions that the lessor company would be required to pay for under operating agreements?

A. I am not prepared to give any amount. Further, I am not an accounting officer but I do have a certain familiarity with the accounts and have worked with the accounting officers and I know there are substantial charges on the Pittsburgh Railway Company's books for those services. It applies to the United Traction Company, the Consolidated Traction Company and possibly ten other underliers.

Hearing closed.

REPORTER'S CERTIFICATE

Commonwealth of Pennsylvania,
County of Allegheny, ss:

I hereby certify that the foregoing pages contain a full, true and complete transcript of my stenographic notes as taken upon the above entitled matter.

Reported by,

Florence V. Ralston.

[fol. 70] TRUSTEES' EXHIBIT No. 1, APRIL 14, 1939

Pittsburgh Railways Company System

Unpaid Federal Income and Excess Profits Taxes and State
Corporate Net Income Taxes for the Calendar Year 1937,
Payable in the Year 1938

	Federal In- come and Excess Profits Taxes Payments Due June 15, September 15, and De- cember 15, 1938	State Corpo- rate Net In- come Taxes, Payment Due May 15, 1938
Allegheny Traction Company	\$ 2,512.41	\$ 875.00
The Citizens Traction Co.	22,820.94	6,312.39
The Suburban Rapid Transit Street Railway Company	6,405.00	1,956.86
Pittsburgh and Birmingham Traction Company	18,852.05	5,260.57
The Duquesne Traction Company	1,251.40	480.55
Federal Street and Pleasant Valley Passenger Railway Company	3,451.20	1,137.50
Mt. Oliver Incline Railway Com- pany	111.04	58.59
Pittsburgh Incline Plane Company	1,383.71	524.69
Monongahela Street Railway Com- pany	40,624.39	11,033.44
Total	\$97,412.14	\$27,639.59

Note:—The foregoing amounts are exclusive of interest.

[fol. 71] TRUSTEES' EXHIBIT No. 2, APRIL 14, 1939

Pittsburgh Railways Company

Unpaid Federal Income Taxes at Source for the Years 1937,
and 1938

Name of Company	1937 (Note A)	1938 (Note B)
The Citizens Traction Co.	\$ 29.00	\$ 5.50
The Suburban Rapid Transit Street Railway Company	96.60	55.20

Name of Company	1937 (Note A)	1938 (Note B)
Pittsburgh and Birmingham Traction Company	6.00	3.00
The Duquesne Traction Company...	63.50	22.00
Federal Street and Pleasant Valley Passenger Railway Company.....	665.16	312.38
The South Side Passenger Railroad Company	3.50	2.50
Penn Street Railway Company.....	16.00	28.00
Pittsburgh Railways Company (Southern Traction Co.).....	2,982.52	1,535.67 (Note C)
Allegheny and Bellevue Street Railway Company	3.00	1.50
Pittsburgh, Allegheny and Manchester Traction Company.....	43.00	17.00
Washington and Canonsburg Railway Company	320.50	151.50
Washington Electric Street Railway Company	53.00	26.50
Ardmore Street Railway Company..	347.50	163.50
Fort Pitt Traction Company.....	552.00	18.50
Pittsburgh, Canonsburg and Washington Railway Company	368.50	129.00
Pittsburgh, Crafton and Mansfield Street Railway Company.....	34.00	11.00
The Pittsburgh Traction Company..	7.00	3.50
Second Avenue Traction Company..	127.00	60.00
The Second Avenue Traction Company	1,201.00	83.50
United Traction Company of Pittsburgh	2,091.25	988.25
West End Traction Company	597.50	465.00
West Liberty and Suburban Street Railway Company	225.00	117.00
Millvale, Etna & Sharpesburgh St. Railway Co.75
Pittsburgh & Charleroi Street Railway Company		3.00
Total	\$9,832.53	\$4,203.75

Note A: Tax became due and payable on June 15, 1938.

Note B: Tax becomes due and payable on June 15, 1939.

Note C: Of this amount, \$110.40 represents tax payable at source on interest paid by the Trustees on Pittsburgh Railways Company Car Trust Bonds.

[fol. 72] TRUSTEES' EXHIBIT No. 3, JULY 6, 1939

W. D. George, Thomas M. Benner and Thomas Fitzgerald,
Trustees

Pittsburgh Railways Company

Debtor under Section 77-B Bankruptcy Act

Income Deduction Items

Amounts of certain items of Income Deductions included in the budget for the period June 1, 1938 to May 31, 1939

compared with the accrual actually made as per preliminary report for the corresponding period.

	Budget	Actual (Preliminary)
Rents:		
Interest on funded debt of leased property		\$1,441,645
Interest on unfunded debt of leased property		137,396
Rentals		830,275
Total Rents	\$2,418,859	\$2,409,316
Taxes of Lessor Companies:		
Federal Income Tax		\$ 119,810
State Corporation Net Income Tax		49,752
Total Taxes of Lessor Companies	\$ 184,874	\$ 169,562
[fol. 73] Miscellaneous (Including tax on Bond Interest):		
Corporate Loan Tax		\$ 44,750
Federal Tax on Bond Interest paid or refunded (Income at Source) on Leased Properties		3,850
Federal Tax on Income at Source		2,825
Miscellaneous		107
Interest during Construction		*4,990
Total Miscellaneous	\$ 85,677	\$ 46,542

July 5, 1939

(* Italic denotes red figures.)

[fol. 74] IN UNITED STATES DISTRICT COURT

SPECIAL MASTER'S REPORT ON PETITION OF TRUSTEES FILED
MARCH 10, 1939 FOR INSTRUCTIONS WITH RESPECT TO TAXES
—Filed August 22, 1939

To the Honorable, the Judges of said Court:

I, Watson B. Adair, to whom as Special Master this matter was referred, respectfully report as follows:

The Hearings

1. Pursuant to the Order of Court of March 10, 1939 and notice given in accordance therewith, I conducted a hearing on March 28, 1939 on "Petition of Trustees of Pittsburgh Railways Company, debtor, and Pittsburgh Motor Coach Company, subsidiary, praying for instructions with respect to certain taxes of the debtor and the subsidiary" filed March 10, 1939. At said hearing, there appeared J. Henry O'Neill and J. Garfield Houston, Esqs., of Blaxter, O'Neill & Houston, attorneys for the trustees; William A. Seifert, William Booth and H. G. Wasson, Jr., Esqs., attorneys for the Philadelphia Company; L. M. Alpern, Esq., attorney for the Tort Creditors Committee; Lee C. Beatty, Esq., attorney for Citizens Traction Company, and Suburban Rapid Transit Street Railway Company; and Hill Burgwin, Esq., for Allegheny Traction Company. After some discussion, the hearing was adjourned to April 14, 1939 when there appeared Messrs O'Neill, Seifert, Booth, Alpern, Beatty and Burgwin, and also A. E. Kountz, Esq., for the Tort Creditors Committee and John D. Ray, Esq., and John E. Shea, [fol. 75] Esq., for the United States Bureau of Internal Revenue, Richard B. Tucker, Jr., Esq., for the City of Pittsburgh, and Mr. Thomas Fitzgerald, one of the trustees. Testimony was taken and the hearing was adjourned to May 15, 1939 when there appeared Messrs. O'Neill, Alpern, Beatty and Kountz. The hearing was then adjourned to May 25, 1939 when there appeared Messrs. O'Neill, Seifert, Booth, Alpern, Kountz and Tucker, and also Richard W. Ahlers, Esq., for Citizens Traction Company, Marland Gale, Esq., for Securities and Exchange Commission, Walter M. Newman, Esq., for Committee for Municipalities' Interest, and Messrs. W. D. George and Thomas Fitzgerald, trustees. The hearing was adjourned to June 9, 1939 when there appeared Messrs. O'Neill, Seifert, Alpern, Kountz, Tucker, Ahlers, Gale and Newman. Messrs W. D. George, Thomas M. Benner and Thomas Fitzgerald, the trustees, were present in person and testimony was taken. The hearing was adjourned to July 6, 1939 when there appeared Messrs. O'Neill, Seifert, Tucker and Ahlers, and Bernard Goodman, Esq. appeared for the Tort Creditors Committee. Further testimony was taken. The transcript of the stenographic notes of the testimony and proceeding is herewith transmitted together with exhibits numbers 1, 2 and 3.

The Objections

2. Written objections were presented by the Tort Creditors Committee to the payment by the trustees of the several taxes due from the underlying companies, which written objections are herewith transmitted. The City of Pittsburgh orally made like objection. The Philadelphia Company took the general position that the taxes of the underliers, as well as the taxes of the debtor and subsidiary should be paid and that unless the taxes of the underliers [fol. 76] were paid, none of the taxes should be paid. The Citizens Traction Company, Suburban Rapid Transit Street Railway Company and Allegheny Traction Company took the same position as the Philadelphia Company. However, the Philadelphia Company opposed the payment of claims against the underlying companies by the Commonwealth of Pennsylvania for corporate income tax on the ground that liability of the underlying companies for such taxes is disputable, and neither the Philadelphia Company nor anyone else appears to object to the payment of the so called Social Security taxes.

The Taxes Involved

3. At the hearing it appeared that in addition to the taxes named in the petition there are other unpaid taxes respecting which instructions are desired. All the taxes respecting which instructions are prayed or desired are the following (the index letters refer to the prayer of the petition):

Taxes Against the Debtor or Its Trustees

United States Taxes

1. Income tax for 1937 withheld at source by debtor
2. Income tax for 1938 withheld at source by debtor
3. Income tax for 1938 withheld at source by trustees
4. Social Security tax, Title VIII (old age benefit) on employes collected by employer for 1939
- 5.(e) Social Security Tax, Title VIII (old age benefit) for 1939
- 6.(e) Social Security Tax, Title IX (unemployment compensation) for 1939
- [fol. 77] 7.(j) Income tax for 1937
- 8.(d) Income tax for 1938

Pennsylvania Taxes

- 9.(a) Capital Stock Tax for 1938
- 10.(c) Corporate Net Income Tax for 1938/
- 11.(b) Corporate Loans Tax for 1938 respecting interest paid by debtor
- 12. Corporate Loans Tax for 1938 respecting interest paid by trustees
- 13.(e) Social Security Tax (unemployment compensation) for 1939

Taxes Against Pittsburgh Motor Coach Company or its Trustees

United States Taxes

- 14.(n) Social Security Tax, Title VIII (old age benefit) for first quarter of 1938
- 15. Social Security Tax, Title VIII (old age benefit on employees collected by employers for 1939
- 16.(m) Social Security Tax, Title VIII (old age benefit) for 1939
- 17.(m) Social Security Tax, Title IX (unemployment compensation) for 1939

Pennsylvania Taxes

- 18.(l) Capital Stock Tax, 1938
- 19.(m) Social Security Tax (unemployment compensation) for 1939

[fol. 78] Taxes Against Underlying Companies

United States Taxes

- 20. Income Tax for 1937 withheld at source
- 21. Income Tax for 1938 withheld at source
- 22.(k) Income Tax for 1937
- 23.(i) Income Tax for 1938

Pennsylvania Taxes

- 24.(f) Capital Stock Tax for 1938
- 25.(h) Corporate Net Income Tax for 1938
- 26.(g) Corporate Loans Tax for 1938

The Facts

4. The principal facts are set forth in the petition and need not here be restated. Additional facts were shown at the hearing.

5. (Items 1, 2, 3, 20, 21). The debtor paid interest in 1937 and 1938 on its own obligations and on obligations of underlying companies containing covenants whereby the obligor agreed to pay the income tax of the obligee up to 2% of such interest, and the Trustees paid interest after May 10, 1938, on obligations of the debtor (ear trust bonds) containing such covenants. All said interest was paid without any actual deduction in respect to federal income tax. The unpaid amounts required by the Revenue Act to be "withheld" at the source respecting interest which was paid in 1937, and 1938, are as follows:

[fol. 79]	Tax on interest paid	
Name of Company	in 1937	in 1938
The Citizens Traction Co.	\$ 29.00	\$ 5.50
The Suburban Rapid Transit Street Railway Company	96.60	55.20
Pittsburgh and Birmingham Traction Company	6.00	3.00
The Duquesne Traction Company	63.50	22.00
Federal Street and Pleasant Valley Passenger Railway Company	665.16	312.38
The South Side Passenger Railroad Company	3.50	2.50
Penn Street Railway Company	16.00	28.00
Allegheny and Bellevue Street Rail- way Company	3.00	1.50
Pittsburgh Allegheny and Manchester Traction Company	43.00	17.00
Washington and Canonsburg Railway Company	320.50	151.50
Washington Electric Street Railway Company	53.00	26.50
Ardmore Street Railway Company	347.50	163.50
Fort Pitt Traction Company	552.00	18.50
Pittsburgh, Canonsburg and Washing- ton Railway Company	368.50	129.00
Pittsburgh, Crafton and Mansfield Street Railway Company	34.00	11.00
[fol. 80]		
The Pittsburgh Traction Company	\$ 7.00	\$ 3.50
Second Avenue Traction Company	127.00	60.00
The Second Avenue Traction Com- pany	1,201.00	83.50

Name of Company	Tax on interest paid	
	in 1937	in 1938
United Traction Company of Pittsburgh	\$2,091.25	\$988.25
West End Traction Company	597.50	465.00
West Liberty and Suburban Street Railway Company	225.00	117.00
Millvale, Etna & Sharpsburg St. Railway Co.	—	.75
Pittsburgh & Charleroi Street Railway Company	—	3.00
(Total on underliers' obligations)	\$6,850.71	\$2,668.08
Pittsburgh Railways Company	2,982.52	1,425.27
Pittsburgh Railways Company interest paid by Trustees after May 10, 1938		110.40
	\$9,832.53	\$4,203.75

The Tax respecting interest paid in 1937 was due and payable on June 15, 1938. The tax respecting interest paid in 1938 was due and payable on June 15, 1939.

6. (Items 1, 2, 3, 20, 21). From and after the dates the several interest payments referred to in paragraph 5 were made, the debtor, the debtor in possession, and the trustees, successively, always had on deposit in Farmers Deposit National Bank, in the account from which interest was paid, a balance larger than the amounts owing for the taxes listed in paragraph 5, plus all unpaid taxes which debtor retained [fol. 81] or collected from interest on wages as required by state or federal law.

7. (Items 7, 8, 10, 22, 23, 25). It does not appear that debtor owes any federal or state income tax for 1937, but the underlying companies owe federal income and excess profits taxes and may owe state corporate net income taxes for 1937 as follows (such taxes for 1938 are shown in Exhibit A attached to the petition):

	Federal In- come and Excess Profits Taxes Payments	Due June 15, September 15, and De- cember 15, 1938	State Corpo- rate Net In- come Taxes, Payment Due May 15, 1938
Allegheny Traction Company	\$ 2,512.41	\$ 875.00	
The Citizens Traction Co.	22,820.94	6,312.39	
The Suburban Rapid Transit Street Railway Company	6,405.00	1,956.86	
Pittsburgh and Birmingham Trac- tion Company	18,852.05	5,260.57	
The Duquesne Traction Company ..	1,251.40	480.55	
Federal Street and Pleasant Valley Passenger Railway Company	3,451.20	1,137.50	
Mt. Olivet Incline Railway Company	111.04	58.59	
Pittsburgh Incline Plane Company ..	1,383.71	524.69	
Monongahela Street Railway Com- pany	40,624.39	11,033.44	
	<u>\$97,412.14</u>	<u>\$27,639.59</u>	

The state corporate net income tax for 1937 was payable [fol. 82] in semi-annual installments, April 15 and September 15, 1938. The April 15, 1938, installment was paid.

8. (Items 4, 5, 15, 16). In paying wages, the trustees are required to deduct 1% for Social Security tax owing by employees under Title VIII of the federal Social Security Act. The Act imposes a tax of the same percentage upon the employer. The taxable wages are approximately \$500,000 per month.

9. (Items 6, 17). The wages taxable under Title IX of the Social Security Act (unemployment compensation) are about \$500,000 per month.

10. (Items 11, 12, 26). The Pennsylvania Corporate Loans Tax for the year 1938, that is, in respect to interest payments made in 1938 prior to May 10, amounts to \$10,442.79 in respect to interest paid on obligations of Pittsburgh Railways Company and \$17,502.56 in respect to interest paid by that company on obligations of underlying companies. Of the total tax, \$27,945.35, the sum of \$302

was actually deducted from the interest paid to bondholders and the remaining was not so deducted. Reports respecting interest on obligations of underlying companies were made by them and the settlements of the amounts owing for the tax were made against them by the state officers. The procedure followed in respect to interest paid by the Pittsburgh Railways Company was as follows: A check was drawn on the debtor's bank account in the Farmers Deposit National Bank to the order of a paying agent for the full amount of the interest payable. Where the paying agent deducted the tax from the amount paid to the bondholder, it, the paying agent, returned to the debtor at the end of each month the amounts so deducted and the debtor deposited such sums in its general account in the [fol. 83] Farmers Deposit National Bank. The balance in that bank from January 1, 1938 to the date when the trustees took possession was always in excess of the amounts so deducted, plus amounts deducted from wages for the Social Security Tax, the lowest balance on deposit being \$51,000. The trustees after May 10, 1938, paid interest on debtor's car trust certificates on which they (if the requirements of the state law are binding on them) were required to deduct \$772 and did deduct \$182, as appears by paragraph 12 of the petition.

11. The Pittsburgh Railways system has been operating as a unified system since 1902. It consists of street railways and inclines belonging to numerous underlying companies and includes buses operated by subsidiary, Pittsburgh Motor Coach Company.

12. The trustees have neither affirmed nor disaffirmed any of the leases or operating agreements under which the Pittsburgh Railways Company has possession of the properties of the several underlying companies.

13. Mr. W. D. George, one of the trustees charged with the duty of preparing a plan, believes that there will not be a great amount of abandonment of properties of underlying companies in the reorganization. He does not consider it practicable at this time for the trustees to say what properties of the underlying companies will and what will not be embraced in the contemplated plan of reorganization.

14. Mr. Fitzgerald, one of the trustees who has been in active charge of the operation of the Pittsburgh Railways

system since 1924, states that since it was created in 1902, there has been absolutely no effort to account for revenues and operating expenses of individual underlying companies, that the most rational approach to a method of doing so [fol. 84] would require an origin and destination statement for each ride taken, and an attempt to do this would be tremendously expensive and would entail so many assumptions as to the allocation of proportions of fares that it could not be used as a dependable basis for allocating revenues to individual companies, that to attempt to apply estimates of operating expenses against any method of estimating earnings would only accumulate additional assumptions and produce a net earnings estimate which would contain a multiplication of errors and therefore have no meaning, that the only way in which the net earnings of each underlier could be determined would be to operate each individually and that this would be of no value in the present problem, would be physically impossible and would not be satisfactory to the public or to the municipal and state authorities.

15. Mr. Fitzgerald further testified that he at present knows of no method of determining what relative rentals should be paid to the various underlying companies whose properties have been utilized by the debtor company or its trustees since May 10, 1938.

16. If the leases and operating agreements were currently effective, the amounts accrued for rental during the period June 1, 1938 to May 31, 1939 would consist of the following items:

Interest on funded debt of leased property— representing the interest on 42 outstanding bond issues of 33 leased companies, of which 27 owned tracks directly	\$1,441,645
Interest on unfunded debt of leased property— being interest on the demand notes of the Con- solidated Traction Company and the United Traction Company held by the Philadelphia Company and the Duquesne Light Company	137,396
[fol. 85] Rentals—being amounts sufficient to pay a certain rate of dividends on stock of 15 underlying companies, 11 of which are in- cluded in the 27 companies above mentioned	830,275
Total	\$2,409,316

If the interest and rentals above mentioned were paid, there would be additional amounts payable for taxes.

17. The Pittsburgh Railways Company has on its books substantial charges against the United Traction Company of Pittsburgh, the Consolidated Traction Company and possibly ten other underlying companies in respect to extraordinary repairs or additions for which the lessor companies may be required to pay under operating agreements or leases, the amounts and merits of which charges have not been shown.

Discussion

18. Taxes accruing during the administration of an estate are payable as expenses of administration: *People of the State of Michigan v. Michigan Trust Company*, 286 U. S. 334, 52 S. Ct. 512 (franchise tax); *Bright v. State of Arkansas* (C. C. A. 8th) 249 F. 950 (franchise tax); *Bear River Paper & Bag Company v. City of Petoskey* (C. C. A. 6th) 241 F. 53 (personal property tax); *Hammond v. Carthage Sulphite Pulp & Paper Company* (C. C. A. 2d) 8 F. (2d) 35 (taxes on property); *Macgregor v. Johnson-Bowdin-Emmerich* (C. C. A. 2d) 39 F. (2d) 574 (real estate taxes); *Central Vermont Railway Company v. Marsch* (C. C. A. 1st) 59 F. (2d) 59 (real estate taxes); *Coy v. Title Guarantee & Trust Company* (D. C. Ore.) 212 F. 520 (personal property tax); *McFarland v. Hurley* (C. C. A. 5th) 286 F. 365 (tax on production of oil). The liability of the [fol. 86] estate for taxes appears also from the Act of Congress which reads as follows:

"State taxation; business conducted by receivers, trustees or other court officers subject to

"Any receiver, liquidator, referee, trustee, or other officers or agents appointed by any United States court who is authorized by said court to conduct any business, or who does conduct any business, shall, from and after June 18, 1934, be subject to all State and local taxes applicable to such business the same as if such business were conducted by an individual or corporation: * * *

U. S. C. A. Title 28, Section 124 a. It follows that the taxes accruing against the debtor, Pittsburgh Railways Company, or the subsidiary, Pittsburgh Motor Coach Company, since May 10, 1938 are expenses of administration.

19. The next question is whether the taxes which constitute administration expenses in the present case should be paid as they become due. When this proceeding began, May 10, 1938, the debtor had \$230,260 cash on hand. That amount increased so that the trustees had cash on hand March 1939 \$1,537,247.46. It is inferred that substantially all of that increase was obtained by the operation of debtor's cars on the tracks of numerous underlying companies. Those companies may assert claims against the estate for this use of their property by the trustees. It has not been shown what are the fair rental values of the several properties or how their actual or relative contributions to the aggregate revenues of the trustees can be ascertained. It is now uncertain whether, on final accounting, there will be enough money or assets wherewith to pay those claims, if and as established, in addition to all the other costs and expenses of administration. There thus [fol. 87] being a possibility that the trusteeship may be or may become insolvent, it is necessary to consider whether payments by the trustees might result in improperly preferring one class of administration creditors, e. g., tax collectors or some trackage owners, to another, e. g., other trackage owners.

20. There is authority for the doctrine that taxes are entitled to priority over other administration expenses: *Atkinson & Co. v. Alrich-Clisbee Co.* 4 D. C. Mass. Morton J.) 248 Fed. 134; *Piedmont Corp. v. Gainesville & N. W. R. Co.* (Dis. Ct. Ga. Sibley J.) 30 F. (2d) 525; *Coy v. Title Guarantee & Trust Company* (C. C. A. 9th) 220 F. 90; *Union Trust Co. v. Illinois M. R. Co.* 117 U. S. 434, 481, 29 L. Ed. 963, 979. Whether or not that be so generally, in the present case it appears equitable that they be given priority over the possible claims of trackage owners for the use of the properties.

21. It is the duty of a common carrier to furnish and operate "a reasonably sufficient number of safe facilities, and run and operate the same with such motive power as may reasonably be required, in the transportation of all such passengers or property as may seek, or be offered to it, for such transportation * * *": *Pennsylvania Act of May 28, 1937 P. L. 1053, Section 403, Pa. Digest, Title 66 Section 1173.* This duty of the underlying com-

panies which own the tracks and franchises has been performed by Pittsburgh Railways Company or its receivers or trustees since 1902. The underlying owner companies are not presently prepared to resume the performance of their duty to the public. Even if they had the necessary capital, cars and personnel, their several properties have for a generation been operated as a unit and by force of circumstances the operation of many of them has become dependent upon the operation of others of them. It can [fol. 88] hardly be doubted that the separate operation of many of the properties of the several owners would be impracticable. Although the underlying companies themselves are not in bankruptcy or reorganization, their properties in reality are in reorganization to the extent that they are in the possession of the trustees, will probably be involved somehow in the reorganization of Pittsburgh Railways Company if any reorganization is effected, and are being operated. That operation appears to be as much for the benefit of the owner companies and their creditors as for the benefit of Pittsburgh Railways Company and its creditors. To the extent that the operation proves profitable, the underliers can be paid something for the use of their properties, probably more than they would have earned separately. Should the profits prove inadequate and the administration be insolvent, there will be nothing for the stockholders and creditors of Pittsburgh Railways Company, except in so far as those creditors have a lien on a minor part of the mileage, but the operation of the system will have preserved or tended to preserve the properties of the owner companies. The operation and management of the properties being for the common benefit, the current expenses thereof should be paid currently even though there ultimately may not be enough to pay the potential separate claims of the owner companies for compensation for the use of their properties.

22. There are many cases in which it has been held that where taxes accrue upon estates in the hands of receivers and are payable as administration expenses, the penalties and interest accruing by reason of delay in payment are likewise payable: *Bright v. State of Arkansas* (C. C. A. 8th) 249 Fed. 950; *Foy v. Title Guarantee Company*, 212 Fed. 520 (penalties only); *McFarland v. Hurley*, 286 Fed. 365 (interest and attorneys' fees); *Ingels v.*

Boteler (C.C. A. 9th) 100 F. (2d) 915. This last case arose [fol. 89] in a bankruptcy in which the Court held that Section 57 j of the Bankruptcy Act did not apply to state tax penalties accruing during administration. The Supreme Court granted a certiorari on April 24, 1939, and a more authoritative ruling may therefore be expected. In the absence of a new ruling to the contrary, it is concluded that penalties and interest have the same status as the taxes upon which they are based. It is therefore desirable that the taxes which are to be paid should be paid promptly.

23. There are further reasons for paying some of the current taxes of the estate:

(a) The trustees have deducted the 1% social security tax from the wages of employes and could not in good conscience, withhold payment thereof to the tax collector.

(b) Unless the contributions owing to the state for social security tax, 2-7/10% of taxable wages, be paid on or before January 31, credit for the amount thereof could not be had as against the federal 3% tax unless it should be held that denial of the provisions of section 902 of the Social Security Act is a penalty and unless the imposition of penalties for delays in payment of taxes be held to be unlawful in the case of trustees.—The penalty in the present case would be severe, possibly \$160,000 per year.

(c) The trustees have deducted Pennsylvania Corporate Loans Tax from some payments of interest, and it would be unconscionable for them to withhold the same from the state.

Taxes on Underliers

24. It is uncertain that any of the leases or operating agreements will ever be accepted by the trustees. Unless [fol. 90] they be accepted, their covenants for payment of taxes will not bind the estate to pay the taxes of the underlying companies as administration expenses. There is no showing that the amounts, if any, owing to the respective companies for the net earnings of their properties or for the use of their properties by the trustees are proportionate to their taxes or even that in every case they are as much as their taxes. Payments of taxes regarded as payments for such earnings or use might give some companies a greater proportion of their dues than others and might even over-

pay some. If the debtor's claims (paragraph 17) against some of the underlying companies be meritorious, they may affect the equities. There does not appear to be any exigency which might justify the risk of effecting preferences or overpayments. It does not seem practicable to deal with the underliers' taxes in the mass, or to dispose of them separately upon the facts shown. At present the taxes of the underliers should not be paid by the trustees.

Particular Taxes

25. The Federal Income Tax for 1938 withheld at the source in respect to interest paid by the trustees on debtor's car trust bonds is governed by Section 143 of the Revenue Acts of 1936 and 1938, that section being the same in each Act. That section does not contemplate the actual deduction of any amount from the interest paid to the creditor but determines the liability of the corporation which has agreed to assume the payee's liability for income tax on the interest received. It is not necessary now to determine whether the corporation's liability is a tax upon it or whether it imposes upon it a liability analogous to that of a tax collector who has collected a tax and is answerable for it, or who has failed to collect a tax which he was bound [fol. 91] to collect. The liability appears to be extended by section 52 of the Revenue Act of 1938 to a corporation's trustee under the Bankruptcy Act and is an expense of administration.

26. The Federal Income Tax for 1937 and 1938 withheld at the source in respect to interest paid by the debtor in 1937 and 1938, under Section 143 of the Revenue Acts of 1936 and of 1938, did not become payable until after May 10, 1938, when this reorganization proceeding began. The question whether the time when the tax became payable, or the time when the interest was paid respecting which the tax accrues, is the test to determine whether the tax was a mere obligation antedating this proceeding or whether it is to be treated as an expense of administration, and the question whether the moneys in the bank to the credit of the debtor, when this proceeding began, included a trust fund which the government can follow and recover, should be determined, if and when presented in a claim by the government. On these questions, if raised, the Court should have the benefit of argument of counsel. It may be

that a present determination of these questions would not be binding in a later contest between the government and the trustees, if there should be such a contest.

27. There does not appear to be any unpaid federal or state Income Tax owing by the debtor for 1937 or 1938.

28. The Pennsylvania capital stock tax is a property tax: *Dupuy v. Johns*, 261 Pa. 40. That tax for 1938 against the debtor and against the subsidiary is an expense of administration.

29. The Pennsylvania Corporate Loans Tax is not a tax upon a corporation but upon the holder of the corporation's obligations: *Commonwealth v. Lehigh V. R. Co.*, 186 Pa. 235. Under the Pennsylvania law, the treasurer of the [fol. 92] Pittsburgh Railways Company, when paying interest on its obligations, was required to deduct from the interest, and thus collect for the state, the corporate loans tax on the obligation upon which the interest was paid; and the corporation is chargeable for its treasurer's omission to do so: *Commonwealth v. Delaware Div. Canal Co.* 123 Pa. 594; *Commonwealth v. Philadelphia R. C. & F. Company*, 137 P. 481. To the extent that actual deductions were made by the debtor's paying agent and returned to the debtor and deposited in its account in the Farmers Deposit National Bank, the trustees appear to have in their hands a trust fund belonging to the Commonwealth of Pennsylvania. It amounts to about \$302, including deductions made from interest paid on obligations of underlying companies, and should be paid.

30. If it be thought that there is a trust fund in the hands of the trustees representing the Corporate Loans Tax for 1938 which the debtor did not deduct but which it had assumed to pay in relief of the obligees, or if it be thought that because the Corporate Loans Tax on interest payments made by the debtor in 1938 was not due until 1939 the liability became an administration expense, the Commonwealth of Pennsylvania may present an appropriate petition upon which the questions can be determined with finality. Unless and until such questions are determined in favor of the Commonwealth, that part of the tax for 1938 should not be treated as a trust fund or as an administration expense.

31. Does the duty of a Pennsylvania corporation to act as tax collector for Pennsylvania devolve upon trustees under the Bankruptcy Act? An Act of Congress, U. S. C. A. Title 28 Section 124, Judicial Code section 65, reads as follows:

“Management of property by receivers. Whenever in [fol. 93] any cause pending in any court of the United States there shall be a receiver or manager in possession of any property, such receiver or manager shall manage and operate such property according to the requirements of the valid laws of the state in which such property shall be situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof. Any receiver or manager who shall wilfully violate any provision of this section shall be fined not more than \$3,000, or imprisoned not more than one year, or both.”

Under a statute relating to liability to suit (U. S. C. A. title 28 sec. 125) a trustee under Section 77B or 77 of the Bankruptcy Act has been held to be a “receiver or manager”: *McGreavy v. Straw* (Sup. Ct. N. H.) 39 A. B. R. (N. S.) 268; *Anderson v. Scandrett*, (Dist. Ct. Minn.) 19 F. Supp. 681; but see *In re Smith* 121 Fed. 1014. Assuming that this statute applies to such trustees, the question arises whether the payment of interest on the debtor's car trust bonds is a part of the management and operation of the property within the meaning of the statute. It has been held that this section 124 applies to a regulation of the rate of fare of street railways: *Westinghouse E. & M. Company v. Binghamton Car Company*, 255 Fed. 378; to an ordinance regulating the speed of trains: *Erb v. Marsch* 177 U. S. 584, 44 L. Ed. 897; to laws imposing liability for injuries to employes in specified circumstances: *Peirce v. Van Dusen*, 78 Fed. 693, *Hornsby v. Eddy* (C. C. A. 8th) 56 Fed. 461; and to a state law requiring distributors of motor vehicle fuel to obtain licenses and to execute bonds for payment of taxes: *Gillis v. State*, 293 U. S. 62, 55 S. Ct. 4. It seems sufficiently clear that the case is within the provisions of Section 124 of Title 28, above quoted, to warrant the view that the estate is liable for the collection of the [fol. 94] Corporate Loans Tax and that it would not be advisable for the trustees to engage in litigation to contest the liability. This tax respecting interest paid by the trustees therefore should be treated as an expense of administration.

32. The Social Security Tax, Title VIII (old age benefit) for the first quarter of 1938 owing by Pittsburgh Motor Coach Company does not appear to be an expense of administration as it accrued and was due and payable prior to May 10, 1938.

Recommendations

I recommend that the trustees of the Pittsburgh Railways Company and of the Pittsburgh Motor Coach Company be instructed as follows:

1. To pay the following taxes owing or to become owing together with any penalties and interest which may have accrued thereon:

Federal Income Tax withheld at the source in respect to interest paid by the trustees

Federal Social Security Tax, Title VIII (old age benefit) for 1939 on employes of the trustees, deductible from wages

Federal Social Security Tax, Title VIII (old age benefit) for 1939 in respect to employes of the trustees

Federal Social Security Tax, Title IX (unemployment compensation) for 1939 in respect to employes of the trustees

Pennsylvania Capital Stock Tax upon Pittsburgh Railways Company and upon Pittsburgh Motor Coach Company for 1938 due in 1939

Pennsylvania Corporate Net Income Tax upon Pittsburgh Railways Company or Pittsburgh Motor Coach Company or the trustees, if any, for 1938, on income earned after May 10

Pennsylvania Corporate Loans Tax for 1938 respecting interest paid by the trustees

Pennsylvania Corporate Loans Tax for 1938 respecting interest paid by debtor, whether on its own obligations or upon the obligations of others, to the extent that the tax was actually deducted by the paying agent from the interest paid and was returned by such agent to the debtor and deposited in debtor's account in Farmers Deposit National Bank, about \$302.

Pennsylvania Social Security Tax (unemployment compensation) for 1939 in respect to employes of the trustees.

2. To refrain from paying the following taxes unless and until otherwise ordered by the Court:

Federal Income Tax for 1937 withheld at the source in respect to interest paid by debtor

Federal Income Tax for 1938 withheld at the source in respect to interest paid by debtor

Pennsylvania Corporate Loans Tax for 1938 respecting interest paid by debtor, except so much of said Tax as was deducted and retained from interest and returned by the paying agent to the debtor and deposited in its account in the Farmers Deposit National Bank.

Social Security Tax, Title VIII (old age benefit) owing by Pittsburgh Motor Coach Company for the first quarter of 1938

[fol. 96] All United States taxes and Pennsylvania taxes against underlying companies.

Respectfully submitted, Watson B. Adair, Special Master.

August 22, 1939.

[fol. 97] IN UNITED STATES DISTRICT COURT

EXCEPTIONS OF PHILADELPHIA COMPANY TO REPORT AND RECOMMENDATIONS OF SPECIAL MASTER—Filed September 11, 1939

To the Honorable, the Judges of said Court:

And, Now, September 11th, 1939, comes the Philadelphia Company, by its counsel, Philip A. Fleger and William A. Seifert, and excepts to the "Special Master's Report on Petition of Trustees of Pittsburgh Railways Company, Debtor, and Pittsburgh Motor Coach Company, Subsidiary, filed March 10, 1939, for Instructions with Respect to Taxes", in respect of the following, to wit:

(a) The conclusion of the Special Master as set forth in Paragraph 24 of his report, to wit:

"It is uncertain that any of the leases or operating agreements will ever be accepted by the trustees. Unless they be accepted, their covenants for payment of taxes will not bind the estate to pay the taxes of the underlying companies as administration expenses. There is no showing that the amounts, if any, owing to the respective companies for the net earnings of their properties or for the use of their

properties by the trustees are proportionate to their taxes or even that in every case they are as much as their taxes. Payments of taxes regarded as payments for such earnings or use might give some companies a greater proportion of their dues than others and might even overpay some. If [fol. 98] the debtor's claims (paragraph 17) against some of the underlying companies be meritorious, they may affect the equities. There does not appear to be any exigency which might justify the risk of effecting preferences or overpayments. It does not seem practicable to deal with the underliers' taxes in the mass, or to dispose of them separately upon the facts shown. At present the taxes of the underliers should not be paid by the trustees."

(b) The conclusion of the Special Master as set forth in paragraph 25 of his report, to wit:

"The Federal Income Tax for 1938 withheld at the source in respect to interest paid by the trustees on debtor's car trust bonds is governed by Section 143 of the Révenue Acts of 1936 and 1938, that section being the same in each Act. That section does not contemplate the actual deduction of any amount from the interest paid to the creditor but determines the liability of the corporation which has agreed to assume the payee's liability for income tax on the interest received. It is not necessary now to determine whether the corporation's liability is a tax upon it or whether it imposes upon it a liability analogous to that of a tax collector who has collected a tax and is answerable for it, or who has failed to collect a tax which he was bound to collect. The liability appears to be extended by section 52 of the Révenue Act of 1938 to a corporation's trustee under the Bankruptcy Act and is an expense of administration."

(c) The conclusion of the Special Master as set forth in Paragraph 26 of his report, to wit:

"The Federal Income Tax for 1937 and 1938 withheld [fol. 99] at the source in respect to interest paid by the debtor in 1937 and 1938, under Section 143 of the Revenue Acts of 1936 and of 1938, did not become payable until after May 10, 1938, when this reorganization proceeding began. The question whether the time when the tax became payable, or the time when the interest was paid respecting which the tax accrues, is the test to determine whether the tax was a mere obligation antedating this proceeding or

whether it is to be treated as an expense of administration, and the question whether the moneys in the bank to the credit of the debtor, when this proceeding began, included a trust fund which the government can follow and recover, should be determined, if and when presented in a claim by the government. On these questions, if raised, the Court should have the benefit of argument of counsel. It may be that a present determination of these questions would not be binding in a later contest between the government and the trustees, if there should be such a contest."

(d) The conclusion of the Special Master as set forth in Paragraph 30 of his report, to wit:

"If it be thought that there is a trust fund in the hands of the trustees representing the Corporate Loans Tax for 1938 which the debtor did not deduct but which it had assumed to pay in relief of the obligees, or if it be thought that because the Corporate Loans Tax on interest payments made by the debtor in 1938 was not due until 1939 the liability became an administration expense, the Commonwealth of Pennsylvania may present an appropriate petition upon which the questions can be determined with finality. Unless and until such questions are determined in favor [fol. 100] of the Commonwealth, that part of the tax for 1938 should not be treated as a trust fund or as an administration expense."

(e) The recommendation of the Special Master that the trustees of the Pittsburgh Railways Company and of the Pittsburgh Motor Coach Company be instructed:

"2. To refrain from paying the following taxes unless and until otherwise ordered by the Court:

Federal Income Tax for 1937 withheld at the source in respect to interest paid by debtor

Federal Income Tax for 1938 withheld at the source in respect to interest paid by debtor

Pennsylvania Corporate Loans Tax for 1938 respecting interest paid by debtor, except so much of said Tax as was deducted and retained from interest and returned by the paying agent to the debtor and deposited in its account in the Farmers Deposit National Bank.

Social Security Tax, Title VIII (old age benefit) owing by Pittsburgh Motor Coach Company for the first quarter of 1938

All United States taxes and Pennsylvania taxes against underlying companies."

As the owner of all of the capital stock of Pittsburgh Railways Company, which company owns all of the capital stock of the Pittsburgh Motor Coach Company, and as the principal creditor of said Pittsburgh Railways Company, the Philadelphia Company respectfully requests leave to file reasons and brief in support of the foregoing exceptions.

[fol. 101] WHEREFORE, your exceptant respectfully submits to your Honorable Court that the above recommendation of the Special Master be not adopted and that the Trustees of the Pittsburgh Railways Company and of the Pittsburgh Motor Coach Company be instructed to pay the following taxes, to wit:

Federal Income Tax for 1937 withheld at the source in respect to interest paid by debtor

Federal Income Tax for 1938 withheld at the source in respect to interest paid by debtor

Pennsylvania Corporate Loans Tax for 1938 respecting interest paid by debtor, except so much of said Tax as was deducted and retained from interest and returned by the paying agent to the debtor and deposited in its account in the Farmers Deposit National Bank

Social Security Tax, Title VIII (old age benefit) owing by Pittsburgh Motor Coach Company for the first quarter of 1938

All United States taxes and Pennsylvania taxes against underlying companies.

Respectfully submitted, Philip A. Fleger, W. A. Seifert, Attorneys for Philadelphia Co.

NOTE.—Exceptions identical to those of the Philadelphia Company were filed on September 11, 1939, jointly by Allegheny, Bellevue and Perrysville Railway Company; The Allenport and Roscoe Electric Street Railway Company; [fol. 102] Ben Avon and Emsworth Street Railway Company; Bon-Air Street Railway Company; Cedar Avenue Street Railway Company; East McKeesport Street Railway Company; Glenwood and Dravosburg Electric Street Railway Company; The McKeesport and Reynoldton Passenger Railway Company; Mt. Washington Street Railway

Company; Mt. Washington Tunnel Company; Pittsburgh, Allegheny, and Manchester Passenger Railway Company; The Pittsburgh, Allegheny and Manchester Traction Company; Pittsburgh and Charleroi Street Railway Company; Pittsburgh and West End Railway Company; Pittsburgh, Canonsburg and Washington Railway Company; Pittsburgh, Crafton and Mansfield Street Railway Company; Pittsburgh, Neville Island and Coraopolis Railway Company; Pittsburgh Union Passenger Railway Company; Second Avenue Passenger Railway Company; Second Avenue Traction Company; The Second Avenue Traction Company; Superior Avenue and Shady Avenue Street Railway Company; United Traction Company of Pittsburgh; Washington and Canonsburg Railway Company; West End Traction Company; West Liberty and Suburban Street Railway Company; West Shore Electric Street Railway Company; Consolidated Traction Company; Ardmore Street Railway Company; Central Passenger Railway Company; The Central Traction Company; Fort Pitt Traction Company; The Pittsburgh Traction Company; The Duquesne Traction Company; The Duquesne Street Railway Company; Federal Street and Pleasant Valley Passenger Railway Company; The Morningside Electric Street Railway Company; Seventeenth Street Incline Plane Company, and are not printed here for the reason that to do so would cause unnecessary duplication and unduly encumber the record.

[fol. 103] IN UNITED STATES DISTRICT COURT

EXCEPTIONS OF CITIZENS TRACTION COMPANY TO REPORT OF
SPECIAL MASTER—Filed September 12, 1939

And now, to wit, September 11, 1939, comes the Citizens Traction Company, by Lee C. Beatty and Richard W. Ahlers, Esquires, its Counsel, and excepts to the Report of the Special Master in the following respects:

First. To the item in paragraph 1 of the "Recommendations" which approves payment of "Pennsylvania Capital Stock Tax upon Pittsburgh Railways Company and upon Pittsburgh Motor Coach Company for 1938, due in 1939", unless the Court also directs payment of like taxes assessed for said period upon exceptant and its wholly owned subsidiary Penn Street Railway Company.

Second. To the item in paragraph 1 of the "Recommendations" which approves payment of "Pennsylvania Corporate Net Income Tax upon Pittsburgh Railways Company or Pittsburgh Motor Coach Company or the Trustees, if any, for 1938 on income earned after May 10" (1938), unless the Court also directs payment of like taxes assessed for said period upon exceptant and its wholly owned subsidiary Penn Street Railway Company.

Third. To the item in paragraph 2 of the "Recommendations" which disapproves payment of "All United States taxes and Pennsylvania taxes against underlying companies" in so far as said recommendation relates to United States taxes and Pennsylvania taxes assessed against [fol. 104] exceptant and its wholly owned subsidiary Penn Street Railway Company.

Citizens Traction Company, Exceptant, by Lee C. Beatty, Richard W. Ahlers, its Attorneys.

NOTE.—Exceptions identical to those of the Citizens Traction Company were filed on September 12, 1939, by The Suburban Rapid Transit Street Railway Company and are not printed here for the reason that to do so would cause unnecessary duplication and unduly encumber the record.

[fol. 105] IN UNITED STATES DISTRICT COURT

EXCEPTIONS AND OBJECTIONS OF THE ALLEGHENY TRACTION COMPANY TO THE REPORT OF SPECIAL MASTER—Filed September 11, 1939

And now, to wit, September 11th, 1939, comes the Allegheny Traction Company by Burgwin, Scully and Churchill, Esquires, its Counsel, and excepts to the report of the Special Master in so far as it relates to his recommendation with regard to the payment of taxes levied and assessed by the United States and the Commonwealth of Pennsylvania against the said Allegheny Traction Company, said recommendation being as follows:

"2. To refrain from paying the following taxes unless and until otherwise ordered by the Court:

All United States taxes and Pennsylvania taxes against underlying companies.”

This exceptant respectfully prays your Honorable Court to refuse to accept the recommendations of the Special Master as hereinbefore set forth and to order and direct the Trustees to pay all United States and Pennsylvania taxes levied and assessed against the Allegheny Traction Company, one of the underlying companies of the debtor.

Hill Burgwin, Burgwin, Scully and Churchill, Counsel for Allegheny Traction Company, Exceptant.

[fol. 106] IN UNITED STATES DISTRICT COURT

JOINDER OF SAMUEL H. PUTNAM IN EXCEPTIONS OF PHILADELPHIA COMPANY ET AL, TO REPORT OF SPECIAL MASTER—Filed September 29, 1939.

To the Honorable, the Judges of Said Court:

And now, September 29, 1939, comes Samuel H. Putnam, a general creditor and owner of securities of underlying companies, and joins in the exceptions to the “Special Master’s Report on Petition of Trustees of Pittsburgh Railways Company, Debtor, and Pittsburgh Motor Coach Company, Subsidiary, filed March 10, 1939, for Instructions with Respect to Taxes”, filed September 11, 1939 by the Philadelphia Company and underlying companies of the Pittsburgh Railways Company.

John M. Reed, Attorney for Samuel H. Putnam.

[fol. 107] IN UNITED STATES DISTRICT COURT

OPINION—Filed October 26, 1939

McVICAR, J.:

This case is before us on exceptions to the Special Master’s report relative to payment of taxes. The Special Master recommended, inter alia, that all taxes assessed against the underliers be not paid at this time. The question argued, (which is the principal question involved) is whether the court should direct the payment of taxes against

the underliers (which are not in dispute) which became due and payable since the approval of the debtors' petition under Sec. 77B of the Bankruptcy Act.

The debtors' petition was filed May 10, 1938 and was approved on the same date. June 14, 1938, permanent trustees were appointed for the debtors, and in said order, the trustees were authorized to

"preserve, maintain, manage and operate and keep in good order, condition and repair, the property and estate in possession of and/or owned by the Debtor, and to manage and conduct its business; and without limiting the generality of the foregoing, to collect and receive the income, rents, revenues, tolls, issues and profits of said property and estate; * * *"

and

"to pay all taxes and assessments due or to become due upon the property in possession of and/or owned by the Debtor; * * *".

[fol. 108] The Pittsburgh Railways Company, since 1902, has operated approximately 1160 miles of street railway, incline plane properties, and through its subsidiary, Pittsburgh Motor Coach Company, a line of buses. Twenty-eight miles of said street railway is owned by the Pittsburgh Railways Company; the remaining 1132 miles is operated by it by virtue of operating agreements and leases from 55 separate underlier companies. The underlying companies own car barns in which the debtors' cars are stored while not in use.

Since approval of debtors' petition, there has become payable to the Commonwealth of Pennsylvania, Social Security Taxes, Corporate Stock Taxes, Corporate Net Income Taxes and Corporate Loan Taxes; also, United States Income Taxes and Social Security Taxes.

March 13, 1939, the trustees of the Pittsburgh Railways Company and Pittsburgh Motor Coach Company, a subsidiary, filed a petition requesting directions in regard to the payment of said taxes, which are more specifically enumerated therein. Objections to the payment of the taxes levied against the underliers were made by the committee representing the tort creditors, and by the City of Pittsburgh for the reasons appearing in paragraph 24 of the Special Master's report. The underlying companies, the

Philadelphia Company and at least one other creditor claimed that said taxes are administration expenses, and that the court should direct the payment thereof. I am of the opinion that the contention of the underlying companies, et al. (with the qualification set forth in the decree filed with this opinion) should be sustained. It will not be necessary to discuss the reasons appearing in the Special Master's report.

As stated before, the Pittsburgh Railways system has [fol. 109] been operated as a unit since the year 1902 and it is still so operated by the trustees. It seems to be generally agreed that any feasible plan of reorganization will have to be based on a unified system. The trustees have ample money from the income received in the operation of said system to pay said taxes. The income received from operation has been kept in one fund and treated as one fund since the system has been operated as a unit, and there is no means, now at least, of determining the income which was received from each of the underliers and from the debtors. The United States is urging payment of the taxes levied against the underlying companies and has intimated at the oral argument of the exceptions to the Special Master's report, in court, that it might distrain in order to collect said taxes. The taxes have always been paid from the income of the unified system, which includes local taxes to the City of Pittsburgh and the County of Allegheny. The local taxes have been paid since the approval of the debtors' petitions. Administration expenses have been recognized as including wages, salaries, cost of supplies, repairs on properties of the underliers, insurance premiums, and for the purchase of leasing of cars used in the system. It is conceded that taxes levied against properties of the debtors should be paid as administration expenses from income received from the entire system, although there is no means of determining how much of that income, if any, should be allocated to the debtor companies.

Orders for payment similar to the order contended for by the underliers, have been made in the cases of American Brake Shoe Co. et al. v. Pittsburgh Railways Company, No. 201, May Term, 1918, in Equity (W. D. Pa.); Philadelphia Rapid Transit Company, debtor, No. 18204 (E. D. of Pa.); Westinghouse Electric & Manufacturing Co. v. Brooklyn Rapid Transit Co., 6 Fed. (2d) 547, (C. C. A. 2).

[fol. 110] The Act of Congress, June 18th, 1934 (28 U. S. C. A. 124 a) provides:

"Any receiver, liquidator, referee, trustee, or other officers or agents appointed by any United States court who is authorized by said court to conduct any business, or who does conduct any business, shall, from and after June 18, 1934, be subject to all State and local taxes applicable to such business the same as if such business were conducted by an individual or corporation * * *"

In *Michigan v. Michigan Trust Company*, 286 U. S. 334, Justice Cardozo, speaking for the Supreme Court, said:

"* * * Taxes owing to the Government, whether due at the beginning of a receivership or subsequently accruing, are the price that business has to pay for protection and security. *Coy v. Title Guarantee & T. Co.* L. R. A. 1915E, 211, 135 C. C. A. 658, 220 Fed. 90, 92. The privilege fees, being taxes, were expenses of administration within the very terms of the order, but in addition they were taxes of such an order that the corporation by failing to pay them became subject, if the State so elected, to a forfeiture of its franchise. Act No. 172 Public Acts 1923 Sec. 7; cf. *Turner v. Western Hydro-Electric Co.*, 241 Mich. 6, 216 N. W. 476. The receiver was under a duty to pay them when they accrued, and having failed to fulfill that duty then, it should be compelled to pay them now. The decisions as to this are persuasive and uniform. *Coy v. Title Guarantee & T. Co.* L. R. A. 1915E, 211, 135 C. C. A. 658, 220 Fed. 90, supra; *Bright v. Arkansas*, 162 C. C. A. 148, 249 Fed. 950; *McFarland v. Hurley* (C. C. A. 5th) 286 Fed. 365; *New York v. Hopkins* (C. C. A. 2d) 18 F. (2d) 731, 733; cf. *Re Tyler*, 149 [fol. 111] U. S. 164, 182, 37 L. Ed. 689, 695, 13 S. Ct. 785."

In *Coy v. Title Guarantee & Trust Co., et al.*, 220 Fed. 90, (C. C. A. 9), it is stated:

"It is too clear for argument that the appointment of a receiver and the taking of property into the hands of the court through its officer does not withdraw it from taxation. It remains subject to assessment and to the payment of all legal taxes thereon while in custodia legis, to the same extent as it was while in the possession of the owner. And

whether or not such taxes be a lien or a debt by the laws of the government within whose jurisdiction the property is situated, such taxes are and should be regarded by the courts as a preferred and paramount claim over all other claims, for they are essential to the existence and maintenance of the very government under which the property is acquired and protected.

“A court”, said Cooley on Taxation (3d Ed.) Vol. 2, p. 834, ‘having in its charge or under its control a fund or other property upon which taxes are due, will, as the representative of the sovereignty, direct them to be paid without raising any question of the means of enforcement by process, and before all other claims except judicial costs. Thus upon proper application and suitable proof a receiver will be ordered to satisfy a tax assessed against the property in his hands, and a like direction will be made in other cases where funds are held subject to the authority of the court.’ ”

In *Bear River Paper & Bag Co. et al. v. City of Petoskey et al.*, 241 Fed. 53 (C. C. A. 6), it is stated:

“We think it unnecessary to decide the question of lien. [fol. 112] These taxes were owing to the state, the county, and the city as the consideration for governmental benefits enjoyed by this property and this business during three years. The property has been in possession of the receivers, and the business has been conducted by them. It is not claimed that any other tax has been assessed in this state against them, or against the property, or against the mortgagor, or mortgagee, or mortgage bondholders. It might have been assessed against the receivers, for C. L. Sec. 3837 (6) says:

“Personal property mortgaged or pledged shall be deemed the property of the person in possession thereof, and may be assessed to him.”

“It is not claimed that the taxes are unjust or in any way inequitable. Under these conditions, and even if it were to be assumed that the taxes had not become a lien against the property, or that, through the mistake of the assessing officers, no enforceable debt against the receivers had arisen, a due regard for the rightful burdens of all citizens and residents toward the state government, and a due recognition of benefits received should impel a federal court to

direct its receiver to make payment. Such payment, in the absence of a meritorious objection to the tax, we regard as the receiver's clear duty; and so it has been held, in substance, if not specifically. In *Re Tyler*, 149 U. S. 164, 187, 13 Sup. Ct. 785, 37 L. Ed. 689; *Coy v. Title Co.* (C. C. A. 9) 220 Fed. 90, 92, 135 C. C. A. 658, L. R. A. 1915E, 211."

See *Gerdes on Corporate Reorganizations*, Sec. 1181; *MacGregor v. Johnson-Cowdin-Emmerich, Inc.*, 39 Fed. (2d) 574 (C. C. A. 2); *Pennsylvania Company for Insurance on Lives, etc. v. Philadelphia Company, etc.*, 266 Fed. 1 [fol. 113] (C. C. A. 3); *Hardee et al. v. American Security & Trust Co.*, 77 Fed. (2d) 382 (C. C. A. Dist. Columbia).

The rule laid down in the above authorities should be applied to taxes levied against the underliers in this case. The system is a unit; it is proposed to reorganize it as a unit; the fund from which the taxes are to be paid arise from this unit; the taxes must be paid ultimately; interest and penalties are accruing by reason of non-payment; the taxes "are the price that business has to pay for protection and security"; "taxes are and should be regarded by the courts as a preferred and paramount claim over all other claims." The same rule should be applied to State and Federal taxes as applies to local taxes. Taxes legally levied against the underliers and which became due and payable after the approval of the original petition are an administration expense and should be ordered paid, subject to the qualification in the decree filed herewith.

IN THE UNITED STATES DISTRICT COURT

ORDER DIRECTING PAYMENT OF TAXES—Filed October 26, 1939

And now, to-wit, October 26th, 1939, this Court, by Order entered March 10, 1939, having referred to Watson B. Adair as Special Master, for a hearing and report thereon, the petition filed March 10, 1939 by W. D. George, Thomas M. Benner and Thomas Fitzgerald, Trustees of Pittsburgh Railways Company, debtor, and of Pittsburgh Motor Coach Company, subsidiary, praying for instructions with respect to the payment of certain taxes; and it appearing that notice of the hearing to be held before the Special Master

and of the hearing to be held by a Judge of this Court upon [fol. 114] the said petition and report of the Special Master and on any exceptions filed thereto was duly given, in accordance with the provisions of the aforesaid Order of Court, to Pittsburgh Railways Company, debtor, and Pittsburgh Motor Coach Company, subsidiary, their creditors, claimants, stockholders and indenture trustees, their subsidiaries and affiliated companies and indenture trustees, under their issues, the Securities and Exchange Commission, the Secretary of the Treasury and all other persons interested in the within reorganization proceeding whose names appear on the books and records of the debtor and its subsidiary; and the hearing before the Special Master having been held and the Special Master having filed his report on said petition, and said petition and report and the exceptions filed thereto having come on for a hearing by a Judge of this Court on October 3, 1939 and having been argued by counsel, and all persons who desired to be heard thereon having been heard; upon consideration thereof, it is ordered, adjudged and decreed as follows:

(a) That W. D. George, Thomas M. Benner and Thomas Fitzgerald, Trustees of Pittsburgh Railways Company, debtor, and of Pittsburgh Motor Coach Company, subsidiary, be and they are hereby instructed and directed to pay the following taxes, together with any penalties and interest which may have accrued thereon:

1. Federal Income Tax for the year 1937 withheld at the source in respect to interest paid by the debtor upon its own obligations and upon the obligations of the underlying companies in the debtor's transportation system.

2. Federal Income Tax for the year 1938 withheld at the source in respect to interest paid by the debtor upon its own obligations and upon the obligations of the underlying companies in the debtor's transportation system, and in respect to interest paid by the Trustees of the debtor.

3. Unpaid balances of Federal Income Taxes of the underlying companies in the debtor's transportation system for the year 1937.

4. Federal Income Taxes of the underlying companies in the debtor's transportation system for the year 1938

except to the extent it shall be determined that such taxes were produced by reason of payments made to underlying companies by the Philadelphia Company in discharge of its obligations as guarantor of the performance of lease covenants.

5. Federal Social Security Tax, Title VIII (old age benefit) for the year 1939 on employees of the Trustees of the debtor and of the subsidiary, deductible from wages.

6. Federal Social Security Tax, Title VIII (old age benefit) for the year 1939 in respect to employees of the Trustees of the debtor and of the subsidiary.

7. Federal Social Security Tax, Title IX (unemployment compensation) for the year 1939 in respect to employees of the Trustees of the debtor and of the subsidiary.

8. Pennsylvania Social Security Tax (unemployment compensation) for the year 1939 in respect to employees of the Trustees of the debtor and of the subsidiary.

9. Pennsylvania Capital Stock Tax of the debtor and of the subsidiary for the year 1938.

10. Pennsylvania Capital Stock Taxes of the underlying companies in the debtor's transportation system for the year 1938.

11. Pennsylvania Corporate Loans Tax for the year 1938 in respect to interest paid by the debtor upon its own [fol. 116] obligations and upon the obligations of the underlying companies in the debtor's transportation system, and in respect to interest paid by the Trustees of the debtor.

12. Pennsylvania Corporate Net Income Taxes of the underlying companies in the debtor's transportation system for the year 1937 (the installment due May 15, 1938), and for the year 1938, when and if it shall be determined in the controversy now pending with the Commonwealth of Pennsylvania that the said underlying companies are liable for the payment of such taxes under the provisions of the Pennsylvania Corporate Net Income Tax Law.

(b) That the exceptions filed to the report of Watson B. Adair, Special Master, upon the aforesaid petition of the Trustees be and they are hereby sustained in so far as they are in accordance with the foregoing provisions of this

Order and are dismissed in so far as they are not in accordance therewith.

By the Court, V.

[fol. 117] IN UNITED STATES DISTRICT COURT

NOTICE OF APPEAL OF TORT CREDITORS' COMMITTEE TO THE
CIRCUIT COURT OF APPEALS—Filed November 25, 1939

To—G. H. BERGER, Clerk:

Notice is hereby given that Walter L. Dipple, James P. McArdle, Ben Paul Brasley and Thomas J. Hoffman, a committee constituted to protect the interests of the persons having claims against the Pittsburgh Railways Company, debtor above named, and Pittsburgh Motor Coach Company, its subsidiary, for causes of action for damages based on negligence in the operation of the business of the debtor and subsidiary and designated as "Tort Creditors' Committee", intervenors in the above entitled proceeding, hereby appeal to the Circuit Court of Appeals for the Third Circuit from the order entered in this proceeding on October 26, 1939, insofar as the same directs the payment of the following taxes:

1. Federal Income Taxes for the year 1937 withheld at the source in respect to interest paid by the debtor upon the obligations of the underlying companies in the debtor's transportation system.
2. Federal Income Taxes for the year 1938 withheld at the source in respect to interest paid by the debtor upon the obligations of the underlying companies in the debtor's transportation system.
3. Unpaid balance of the Federal Income Taxes of the [fol. 118] underlying companies in the debtor's transportation system for the year 1937.
4. Federal Income Taxes of the underlying companies in the debtor's transportation system for the year 1938.
5. Pennsylvania Capital Stock Taxes of the underlying companies in the debtor's transportation system for the year 1938.

6. Pennsylvania Corporate Loan Taxes for the year 1938 in respect to interest paid by the debtor upon the obligations of the underlying companies in the debtor's transportation system.

7. Pennsylvania Corporate Net Income Taxes of the underlying companies in the debtor's transportation system for the year 1937 and the year 1938.

A. E. Kountz, Lewis M. Alpern, Attorneys for Appellants, Walter L. Dipple, James P. McArdle, Ben Paul Brasley and Thomas J. Hoffman, Tort Creditors' Committee.

[fol. 119] IN UNITED STATES DISTRICT COURT

NOTICE OF APPEAL OF CITY OF PITTSBURGH TO THE CIRCUIT COURT OF APPEALS—Filed November 25, 1939

Notice is hereby given that the City of Pittsburgh hereby appeals to the United States Circuit Court of Appeals for the Third Circuit from those parts of the order entered on October 26, 1939, which direct the Trustees to pay the taxes of the underlying companies, more particularly the following parts of said order insofar as they relate to any taxes of the various underlying companies:

Sections (a) 1, (a) 2, (a) 3, (a) 4, (a) 10, (a) 11, and (a) 12.

Wm. Alvah Stewart, Solicitor for City of Pittsburgh.

November 25, 1939.

[fol. 120] IN UNITED STATES DISTRICT COURT

DESIGNATION OF CONTENTS OF RECORD ON APPEAL—Filed December 13, 1939

And now, to-wit, December 13, 1939, come the City of Pittsburgh and the Tort Creditors Committee, appellants, and designate the following portions of the record, proceedings and evidence as the Record on Appeal from the Order of Court of October 26, 1939, directing the payment of certain taxes:

1. Relevant Docket entries as approved by order of Court of December 11, 1939, and the Order of Court of December 11, 1939.

2. Trustees' petition for instructions with respect to certain taxes of the debtor and the subsidiary and the order of reference filed March 10, 1939.

3. Objections of the Tort Creditors Committee to the payment of certain tax items, filed April 14, 1939.

4. All of the evidence taken before the Special Master, filed August 22, 1939, omitting only the discussions of counsel found on the following pages of the transcript: pages 3 to 10 inclusive; pages 21 to 39 inclusive; pages 71 to 75 up to the testimony of W. D. George.

5. Trustees' Exhibits Nos. 1, 2 and 3.

6. Special Master's Report, filed August 22, 1939.

7. Exceptions of Philadelphia Company to Master's Report, filed September 11, 1939.

[fol. 121] 8. The following statement to be printed:

"Exceptions identical to those of the Philadelphia Company were filed on September 11, 1939, jointly by Allegheny, Bellevue and Perrysville Railway Company; The Allentown and Roscoe Electric Street Railway Company; Ben Avon and Emsworth Street Railway Company; Bon-Air Street Railway Company; Cedar Avenue Street Railway Company; East McKeesport Street Railway Company; Glenwood and Dravosburg Electric Street Railway Company; The McKeesport and Reynoldton Passenger Railway Company; Mt. Washington Street Railway Company; Mt. Washington Tunnel Company; Pittsburgh, Allegheny, and Manchester Passenger Railway Company; The Pittsburgh, Allegheny and Manchester Traction Company; Pittsburgh & Charleroi Street Railway Company; Pittsburgh and West End Railway Company; Pittsburgh, Canonsburg and Washington Railway Company; Pittsburgh, Crafton and Mansfield Street Railway Company; Pittsburgh, Neville Island and Coraopolis Railway Company; Pittsburgh Union Passenger Railway Company; Second Avenue Passenger Railway Company; Second Avenue Traction Company; The Second Avenue Traction Company; Superior Avenue and Shady Avenue Street Railway Company; United Traction Company of Pittsburgh; Washington and Canonsburg Rail-

way Company; West End Traction Company; West Liberty and Suburban Street Railway Company; West Shore Electric Street Railway Company; Consolidated Traction Company; Ardmore Street Railway Company; Central Passenger Railway Company; The Central Traction Company; [fol.122] Fort Pitt Traction Company; The Pittsburgh Traction Company; The Duquesne Traction Company; The Duquesne Street Railway Company; Federal Street and Pleasant Valley Passenger Railway Company; The Morningside Electric Street Railway Company; Seventeenth Street Incline Plane Company, and are not printed here for the reason that to do so would cause unnecessary duplication and unduly encumber the record."

9. Exceptions of The Allegheny Traction Company to Master's Report, filed September 11, 1939.

10. Exceptions of Citizens Traction Company to Master's Report, filed September 12, 1939.

11. The following statement to be printed:

"Exceptions identical to those of the Citizens Traction Company were filed on September 12, 1939, by The Suburban Rapid Transit Street Railway Company and are not printed here for the reason that to do so would cause unnecessary duplication and unduly encumber the record."

12. Joinder in exceptions to Master's Report by Samuel H. Putnam, filed September 29, 1939.

13. Opinion of Judge McVicar, filed October 26, 1939.

14. Order of Court, filed October 26, 1939.

15. Notice of Appeal of Tort Creditors Committee, filed November 25, 1939.

16. Notice of Appeal of City of Pittsburgh, filed November 25, 1939.

[fol.123] 17. Designation of Contents of Record, filed December 13, 1939.

18. Designation of Appellants points, filed December 13, 1939.

19. Certificate of Clerk.

Wm. Alvah Stewart, Attorney for the City of Pittsburgh, Appellant.

A. E. Kountz, Lewis M. Alpern, Attorneys for Tort Creditors Committee, Appellant.

STATEMENT OF APPELLANTS' POINTS ON APPEAL—Filed December 13, 1939

And now, to-wit, December 13, 1939, the City of Pittsburgh and the Tort Creditors Committee, appellants from the order of court of October 26, 1939, directing the Trustees of Pittsburgh Railways Company, debtor, to pay certain taxes, hereby designate the following points as the points on which they intend to rely on the appeal:

1. That the court erred in directing the payment of taxes accrued against the underlying companies which were due and owing prior to May 10, 1938, the date of the filing of the petition for reorganization, for the reason that said items were at no time and are not administration expenses during reorganization and are not tax obligations of the debtor entitled to priority in payment over the claims of unsecured creditors, but are mere contract obligations of the debtor on a parity with the other unsecured claims against the debtor.

2. That the court erred in holding that by virtue of the unified operation of the debtor's railway system the Trustees' obligation to pay the taxes accrued against the underlying companies during the period of administration and reorganization is a tax obligation of the debtor in possession and of the Trustees and, therefore, payable as taxes of the debtor company.

3. That inasmuch as the Trustees have not as yet either affirmed or rejected the executory contracts between the debtor corporation and the several underliers or any of [fol. 125] them whereby the debtor obligated itself to pay, inter alia, the taxes of the underliers in question, the court erred in failing to hold that unless and until the several leases and operating agreements are affirmed, the only claim of the underliers during the period of administration in reorganization is for use and occupancy.

4. That inasmuch as the measure of use and occupancy in public utility reorganization cases is the net earnings realized from the operation of the lessors' properties, the court erred in directing the Trustees to pay the taxes accrued against the debtor's underlying companies during

the administration in reorganization without requiring proof that the net earnings attributable to each of the underliers is equal to or in excess of the taxes of each of them.

5. That the payment of the underliers taxes incurred during the period of administration in reorganization without the establishing of the earnings of each underlier's property may cause preferences and over-payments.

6. That there are no special equities which would warrant the District Court in refusing to apply the general rules applicable to the payment of use and occupancy by Trustees in reorganization of public utility companies.

Wm. Alvah Stewart, Attorney for City of Pittsburgh.
A. E. Kountz, Lewis M. Alpern, Attorneys for Tort Creditors Committee.

[fol. 126] IN UNITED STATES DISTRICT COURT

ORDER OF COURT AND STIPULATION—Filed December 22, 1939

And now, to-wit, this 22nd day of December, 1939, upon motion of counsel and after due consideration, it is ordered that the time for the filing of the record on appeal with the Clerk of the Circuit Court of Appeals in the appeals of the City of Pittsburgh and the Tort Creditors Committee from an Order entered by this Court on October 26, 1939, be extended from January 4, 1940 to January 18, 1940, provided that both the typewritten and printed record be filed on or before January 18, 1940.

By the Court, V.

And now, to-wit, December 22, 1939, it is hereby stipulated by the City of Pittsburgh and the Tort Creditors Committee, through their respective counsel, that their printed brief or briefs will be filed on or before February 3, 1940.

Richard B. Tucker, Jr., Attorney for City of Pittsburgh.

Lewis M. Alpern, Attorney for Tort Creditors Committee.

[fol. 127] IN UNITED STATES DISTRICT COURT

ORDER OF COURT AND EXCEPTION—Filed December 22, 1939

And now, to-wit, December 22nd, 1939, upon consideration of the foregoing motion of Blaxter, O'Neill & Hous-

ton, counsel for W. D. George, Thomas M. Benner and Thomas Fitzgerald, Trustees of Pittsburgh Railways Company, debtor, and Pittsburgh Motor Coach Company, subsidiary, it is ordered that there be filed and docketed in the office of the Clerk of this Court and made a part of the record in this proceeding the "Recommendation of Counsel For Trustees Relative To Trustees Petition For Instructions With Respect To Certain Taxes" which Blaxter, O'Neill & Houston filed with McVicar, J. personally on or about October 20, 1939, pursuant to his direction so to do, and which document does not appear to have heretofore been filed and docketed in the office of the Clerk of this Court.

By the Court, V.

Ex die exception noted to City of Pittsburgh and Tort Creditors Committee.

McVicar, D. J.

[fol. 128] IN UNITED STATES DISTRICT COURT

DESIGNATION OF ADDITIONAL PORTIONS OF THE RECORD, PROCEEDINGS AND EVIDENCE TO BE INCLUDED IN THE RECORD ON APPEAL—Filed December 22, 1939

And now, to-wit, December 22, 1939, come W. D. George, Thomas M. Benner and Thomas Fitzgerald, Trustees of Pittsburgh Railways Company, debtor, and Pittsburgh Motor Coach Company, subsidiary, and designate as an additional portion of the record, proceedings and evidence to be included in the record on appeal, and also as an additional docket entry to be included in the list of docket entries to be printed, in the manner and form it may be docketed, the following:

"Recommendations of Counsel for Trustees Relative to Trustees' Petition for Instructions with Respect to Certain Taxes."

Blaxter, O'Neill & Houston, Counsel for W. D. George, Thomas M. Benner and Thomas Fitzgerald, Trustees of Pittsburgh Railways Company, Debtor, and Pittsburgh Motor Coach Company, Subsidiary.

[fol. 129] IN UNITED STATES DISTRICT COURT

RECOMMENDATIONS OF COUNSEL FOR TRUSTEES RELATIVE TO
TRUSTEES' PETITION FOR INSTRUCTIONS WITH RESPECT TO
CERTAIN TAXES—Filed December 22, 1939

To the Honorable, the Judges of said Court:

Blaxter, O'Neill & Houston, counsel for W. D. George, Thomas M. Benner and Thomas Fitzgerald, Trustees of Pittsburgh Railways Company, debtor, and of Pittsburgh Motor Coach Company, subsidiary, submit herewith, pursuant to the request of your Honorable Court, their recommendations with respect to the Trustees' petition filed March 10, 1938 praying for instructions as to the payment of certain State and Federal taxes and the report of the Special Master thereon.

In his report the Special Master, in substance, recommended that certain of the taxes of the debtor or its Trustees concerning which instructions were asked, be paid in full by the Trustees and others only in part; and he recommended that none of the taxes of the underlying companies be paid unless and until otherwise ordered by the Court.

Whatever may be the technical legal relationship existing between Pittsburgh Railways Company and its underlying street railway and incline plane companies, in point of fact and for all practical purposes all those companies have been operated as a single and unified transportation system since 1902, and they are now being operated as such by the Trustees of Pittsburgh Railways Company, debtor. The [fol. 130] operation of the business of the several companies as a unified system was brought about by the voluntary action of those companies.

The plan of reorganization being developed by the two Trustees of the debtor who were directed to prepare and file a plan of reorganization for the debtor contemplates the formation of a new company which will acquire title to the properties of the underlying companies included in the Pittsburgh Railways Company transportation system and the operation thereof by the new company as a unified system. At the hearing before the Special Master, W. D. George, one of the reorganization Trustees, testified that most of the properties which are now in use will continue in use in the reorganized system.

Taxes Against the Debtor or Its Trustees

The Master recommended payment in full of all taxes owing by the debtor or its Trustees concerning which instructions were asked, except Federal Income Tax withheld at source for the years 1937 and 1938 and Pennsylvania Corporate Loans Tax for the year 1938, and these particular taxes, after a consideration of certain technical features involved, he recommended be paid only in part. It is true that some technical questions are involved with respect to these particular taxes, but in our opinion they should not be allowed to control the basic fact that the full amount of the taxes became due and payable subsequent to May 10, 1938, the date of filing of the debtor's petition, and are, therefore, expenses of administration, and for that reason, as well as for the reasons hereinafter stated as to why underliers' taxes should be paid, these particular taxes likewise should be paid in full by the Trustees. *Florida National Bank of Jacksonville vs. United States*, 87 Fed. (2d) 896; *Prudential Insurance Co. of America [fol. 131] vs. Liberdar Holding Co.*, 74 Fed. (2d) 50; *People of Michigan vs. Michigan Trust Co.*, 286 U. S. 334, 52 S. Ct. 512.

Taxes Against Underlying Companies

The reasons stated by the Master in support of his recommendation with respect to the taxes of underlying companies appear in paragraph 24 of his report, wherein he says:

"It is uncertain that any of the leases or operating agreements will ever be accepted by the trustees. Unless they be accepted, their covenants for payment of taxes will not bind the estate to pay the taxes of the underlying companies as administration expenses. There is no showing that the amounts, if any, owing to the respective companies for the net earnings of their properties or for the use of their properties by the trustees are proportionate to their taxes or even that in every case they are as much as their taxes. Payments of taxes regarded as payments for such earnings or use might give some companies a greater proportion of their dues than others and might even overpay some. If the debtor's claims (paragraph 17) against some of the underlying companies be meritorious, they may affect the equities. There does not appear to be any exigency which

might justify the risk of effecting preferences or overpayments. It does not seem practicable to deal with the underliers' taxes in the mass, or to dispose of them separately upon the facts shown. At present the taxes of the underliers should not be paid by the trustees."

After careful consideration of the Master's report, and having had the benefit of the exhaustive briefs that were filed with the Court and the oral arguments made in Court [fol. 132] by counsel for interested parties at the hearing upon the exceptions filed to the Master's report, Counsel for the Trustees have come to the conclusion that the Master related the matter of the payment of the underliers' taxes too closely to payments that might possibly be due underlying companies on account of use and occupancy of their properties. In other words, he did not, in our opinion, attach sufficient importance to the fact that the properties of the underlying companies are in the possession of the Trustees and are being used and operated by them with properties of the debtor as a unified system, and therefore the taxes of the underlying companies are, in effect, taxes of the unified system and, as such, operating and administrative expenses of the Trustees; and also that the Master was in error in concluding that it was not practicable to deal with the underliers' taxes in the mass. Moreover, with respect to public utility companies, the measure of the value of the use and occupancy of the properties during the administration by receivers or trustees is held to be the net earnings derived from the properties during the period, and it should be noted that it was testified at the hearing before the Master that it is not possible to determine the net earnings of the separate underliers in the Pittsburgh Railways system. We have found no case in which it was decided that a receiver or a trustee of a railway company should not pay the taxes of an underlying company included as part of a railway system being operated by the receiver or trustee unless the net earnings of the underlying company were equal to or in excess of the amount of such taxes.

It is very important to note that at the hearing before the Court upon the exceptions to the Master's report, 45 underlying companies, including all the important underliers in the Pittsburgh Railways system, urged payment of [fol. 133] the underliers' taxes in the mass, without regard

to whether the taxes paid for any underlier might ultimately exceed the amount, if any, which said underlier would be entitled to receive for use and occupancy of its properties by the Trustees. It is therefore apparent that the underlying companies, comprising by far the major part of the system, recognize that they function as part of a unified transportation system, and that with respect to operating expenses they are to be dealt with, not as units or individually but in the mass,—that from an operating standpoint, they have no separate identity. The Master did not have the advantage of this expression of the attitude of such a great number of the underliers when this matter was before him.

All taxes against the underlying companies concerning which recommendations were made by the Master were taxes which became due and payable subsequent to May 10, 1938, the date of the filing of the debtor's petition herein.

In our opinion, all taxes of underlying companies should be paid in full by the Trustees of the debtor as an administration expense (subject to the qualifications hereinafter stated with respect to Federal Income Taxes for the year 1938 and State Corporate Net Income Taxes for the years 1937 and 1938) for the following reasons:

1. The properties of the debtor and of the underlying companies since 1902 have been and are now being operated as a unified transportation system for the benefit of all, and the revenues produced from the operation of these properties have always been expended for the maintenance and operation of the system as a whole, without regard to the particular source of the revenues. No attempt was ever made to account for what revenues or earnings, if any, were produced by the operation of the properties of any particular underlier. It would seem to be clearly inequitable [fol. 134] for the Trustees to pay taxes of the debtor from revenues unquestionably produced in large part from the operation of underliers' properties and not to pay the taxes of the underliers. The Trustees are, moreover, out of the common funds, maintaining and keeping in repair all of the properties, purchasing equipment and supplies for the system, paying wages and salaries and all other operating expenses, and, on equitable grounds alone, there would seem to be no reason to discriminate with respect to the taxes of the system.

2. It is well settled that taxes accruing upon estates in the hands of receivers or trustees are payable as administration expenses, and that the interest and penalties accruing by reason of delay in payment are likewise payable. In *re Preble Corporation*, 15 Fed. Supp. 775; *Coy vs. Title Guarantee & Trust Co.*, 220 Fed. 90; *People of Michigan vs. Michigan Trust Co.*, 286 U. S. 334; 52 S. Ct. 512; *Ingels vs. Boteler*, 100 Fed. (2d) 915. Although the underlying companies as corporate entities are technically not before the Court in the reorganization proceeding, their properties are, nevertheless, in the possession of the Trustees pursuant to an Order of this Court, and the Trustees are operating said properties and exercising the franchises of the underlying companies in connection with and as part of the operation of the debtor's business. Therefore, in a very real sense and, we believe, in a legal sense, their properties are part of the estate being operated and administered by the Trustees of the debtor and their taxes are as much administration expenses as the debtor's own taxes.

3. If the taxes of underliers are not paid, interest will continue to accrue thereon,—in some instances at as high a rate as 12% per annum;—and will, no doubt, become liens against the underliers' properties. As hereinbefore stated, the reorganization trustees contemplate that under the plan which they propose to file, a new company is to acquire all [fol. 135] the properties of the debtor and its underliers. It would seem, therefore, that any taxes which are owed by the underlying companies or which may have become liens against their properties would ultimately have to be dealt with.

4. From the beginning of this proceeding the Trustees have been paying real estate taxes assessed against underlying companies by Allegheny County, the City of Pittsburgh and other municipalities. As the legal objections which are made to the payment of the other taxes of underliers herein considered do not appear to be persuasive, it would seem to be fair and equitable to accord like treatment to all taxing authorities.

5. The Trustees have in their possession sufficient cash funds derived from the operation of the system with which to pay in full, with any penalties or interest that may have

accrued thereon, all taxes the payment of which is recommended herein.

Qualifications With Respect to Underlying Companies' Federal Income Taxes for the Year 1938 and State Corporate Net Income Taxes for the Years 1937 and 1938

As to Federal Income Taxes of the underlying companies for the year 1938 which became due and payable in installments on and after March 15, 1939, attention is called to the fact that a part of the taxes in this group are produced by reason of the fact that the Philadelphia Company paid certain sums of money to or for the account of certain underlying companies in discharge of rental obligations under certain leases of properties heretofore operated by the debtor and now operated by the Trustees; and such payments have created taxable income to the underlying companies receiving such payments. While it is true that the [fol. 136] Pittsburgh Railways Company had contracted to pay the rental obligations and that the position of the Philadelphia Company with respect thereto is that of a guarantor, yet the Trustees have not affirmed these leases. It would therefore seem that the payments made by the Philadelphia Company were in discharge of its own obligations and not those of the Trustees. Since the Trustees are not paying any rentals to underlying companies, it does not seem fair and equitable to apply the general funds in the hands of the Trustees produced by all the underliers for payment of an income tax liability which would not have existed except for the performance of the obligations of the Philadelphia Company.

As to the second installment of State Corporate Net Income Tax for the year 1937 which became due and payable May 15, 1938, and as to the State Corporate Net Income Tax for the year 1938 which became due and payable in installments April 15, 1939 and May 15, 1939, respectively, we are of the opinion that these taxes should not be paid at this time for the reason that liability of the underlying companies therefore is disputed and a controversy with respect thereto is now pending.

Taxes Against Pittsburgh Motor Coach Company or Its Trustees

As to the taxes of Pittsburgh Motor Coach Company or its Trustees, the Master has recommended payment of said

taxes in full, with any penalties and interest which may have accrued thereon, except as to Social Security Tax, Title VIII (old age benefit—employer's share), owing by Pittsburgh Motor Coach Company for the first quarter of 1938. In our opinion, the Master's conclusions with respect to all the taxes under this heading are correct. The one item which he recommended be not paid is, obviously, a tax [fol. 137] which became due and payable prior to May 10, 1938 and is simply a debt of Pittsburgh Motor Coach Company.

Our Recommendations

I. The Master has recommended that the Trustees of the Pittsburgh Railways Company and of the Pittsburgh Motor Coach Company be instructed to pay the following taxes owing or to become owing, together with any penalties and interest which may have accrued thereon. Our recommendation with respect to each of said taxes is set forth under the particular tax.

(a) Federal Income Tax withheld at the source in respect to interest paid by the trustees.

We recommend payment of this tax.

(b) Federal Social Security Tax, Title VIII (old age benefit) for 1939 on employes of the trustees, deductible from wages.

We recommend payment of this tax.

(c) Federal Social Security Tax, Title VIII (old age benefit) for 1939 in respect to employes of the trustees.

We recommend payment of this tax.

(d) Federal Social Security Tax, Title IX (unemployment compensation) for 1939 in respect to employes of the trustees.

We recommend payment of this tax.

(e) Pennsylvania Capital Stock Tax upon Pittsburgh Railways Company and upon Pittsburgh Motor Coach Company for 1938 due in 1939.

We recommend payment of this tax.

[fol. 138] (f) Pennsylvania Corporate Net Income Tax upon Pittsburgh Railways Company or Pittsburgh Motor

Coach Company or the trustees, if any, for 1938, on income earned after May 10.

We recommend payment of this tax, if any.

It is our understanding no tax is owing.

(g) Pennsylvania Corporate Loans Tax for 1938 respecting interest paid by the trustees.

We recommend payment of this tax.

(h) Pennsylvania Corporate Loans Tax for 1938 respecting interest paid by debtor whether on its own obligations or upon the obligations of others, to the extent that the tax was actually deducted by the paying agent from the interest paid and was returned by such agent to the debtor and deposited in debtor's account in Farmers Deposit National Bank, about \$302.

We recommend payment of the full tax respecting interest paid by debtor whether upon its own obligations or upon the obligations of others, and do not limit our recommendation only to the tax that was actually deducted by the paying agent from the interest paid and returned by such agent to the debtor.

(i) Pennsylvania Social Security Tax (unemployment compensation) for 1939 in respect to employees of the trustees.

We recommend payment of this tax.

II. The Master has recommended that the Trustees of the Pittsburgh Railways Company and of the Pittsburgh Motor Coach Company be instructed to refrain from paying [fol. 139] the following taxes unless and until otherwise ordered by the Court. Our recommendation with respect to each of said taxes is set forth under the particular tax.

(a) Federal Income Tax for 1937 withheld at the source in respect to interest paid by debtor.

We recommend payment of this tax.

(b) Federal Income Tax for 1938 withheld at the source in respect to interest paid by debtor.

We recommend payment of this tax.

(c) Pennsylvania Corporate Loans Tax for 1938 respecting interest paid by debtor, except so much of said tax as

was deducted and retained from interest and returned by the paying agent to the debtor and deposited in its account in the Farmers Deposit National Bank.

We recommend payment of the tax in full.

See our recommendation at I (h).

(d) Social Security Tax, Title VIII (old-age benefit) owing by Pittsburgh Motor Coach Company for the first quarter of 1938.

We do not recommend payment of this tax.

(e) All United States taxes and Pennsylvania taxes against underlying companies.

We recommend payment of these taxes with the following qualifications:

1 As to Federal Income Taxes of the underlying companies for the year 1938, we recommend payment of said taxes except to the extent it may be determined that such taxes were produced by reason of payments made to un-[fol. 140] derlying companies by the Philadelphia Company in discharge of its obligations as guarantor of the performance of lease covenants.

2. As to State Corporate Net Income Taxes, we recommend that the taxes be not paid unless and until it should be determined that the underlying companies are liable therefor.

Respectfully submitted, Blaxter, O'Neill & Houston,
Counsel for the Trustees.

[fol. 141] IN UNITED STATES DISTRICT COURT

STIPULATION RE ADDITIONAL PARTS OF RECORD ON APPEAL—
Filed December 29, 1939

It is hereby stipulated that the following additional portions of the record shall be printed in the Record on Appeal in the Appeals of the City of Pittsburgh and the Tort Creditors' Committee from the Order of the above Court dated October 26, 1939, directing the payment of certain taxes:

1. The following docket entries relevant to the appeals in addition to those which have been heretofore designated by the appellants:

Dec. 11, On petition order made authorizing the City of Pittsburgh and the Tort Creditors Committee to print in the record on appeal from the order of Court of Oct. 26, 1939, directing the Trustees of the debtor company to pay certain taxes, only the docket entries set forth in Exhibit "A" attached to petition, in lieu of the docket entries on the record except such other docket entries as the appellees may designate with the approval of the Court.

Dec. 11, Acceptance of service of notice as to printing the record on appeal filed.

Dec. 13, Statement of Appellants' (City of Pittsburgh and the Tort Creditors' Committee) Points on Appeal filed. [fol. 142] Dec. 13, Designation of Contents of Record on Appeal (City of Pittsburgh and Tort Creditors' Committee) filed.

Dec. 13, Transcripts of Testimony (2) taken March 28, 1939 at hearing on Petition of Trustees Respecting Taxes and Adjournments thereof, filed.

Dec. 14, Acceptance of service of notice of filing Designation of Contents of Record on Appeal and Statement of Points, filed.

Dec. 22, Recommendations of counsel for trustees relative to Trustees' Petition for Instructions with Respect to Certain Taxes filed.

Dec. 22, Designation of Additional Portions of the Record, proceedings and Evidence to be included in the Record on Appeal and Notice and Acceptance of Service filed.

Dec. 22, Order made directing that the time for filing of the record on appeal with the Clerk of the Circuit Court of Appeals in the appeals of the City of Pittsburgh and the Tort Creditors Committee from an order entered by this Court on Oct. 26, 1939 be extended from Jan. 4, 1940 to Jan. 18, 1940, provided that both the typewritten and printed record be filed on or before Jan. 18, 1940.

Dec. 22, On petition order made directing that there be filed and docketed in the office of the Clerk and made a part of the record in this proceeding the "Recommendation of Counsel for Trustees Relative to Trustees Petition for Instructions with Respect to Certain Taxes" which Blaxter, [fol. 143] O'Neill & Houston filed with McVicar, J. person-

ally on or about October 20, 1939, which document does not appear to have heretofore been filed and docketed in the office of the Clerk of this Court.

Same day exception noted to City of Pittsburgh and Tort Creditors Committee.

Dec. 29, Stipulation of counsel as to additional portions of the record that shall be printed in the Record on Appeal in the appeals of the City of Pittsburgh and the Tort Creditors' Committee, filed.

2. Order of Court dated December 22, 1939, extending the time for filing the Record on Appeal and the stipulation of counsel for the City of Pittsburgh and for the Tort Creditors' Committee appended thereto.

3. Order of Court dated December 22, 1939, directing that there be filed and docketed in the office of the Clerk of the Court, and made a part of the record in the proceeding, the "Recommendations of Counsel for Trustees Relative to Trustees Petition for Instructions with Respect to Certain Taxes," and the exception thereto.

4. Trustees designation of additional portions of the record, proceedings and evidence to be included in the Record on Appeal, filed December 22, 1939.

5. The "Recommendations of Counsel for Trustees Relative to Trustees' Petition for Instructions with Respect to Certain Taxes," without prejudice to the right of the City of Pittsburgh and the Tort Creditors Committee, Appellants, to urge the exception noted to them on the Order of Court dated December 22, 1939, directing that there be filed [fol. 144] and docketed in the office of the Clerk of the Court and made part of the record in the proceeding the aforesaid "Recommendations."

6. The within stipulation.

Leon Wald, Attorney for City of Pittsburgh. A. E. Kountz, Lewis M. Alpern, Attorneys for Tort Creditors Committee. Blaxter, O'Neill & Houston, Attorneys for Trustees. Reed, Smith, Shaw & McClay, by W. A. Seifert, Attorneys for Philadelphia Company and Underliers.

[fol. 145] Clerk's Certificate to foregoing transcript omitted in printing.

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[fol. 146] IN THE UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE THIRD CIRCUIT, OCTOBER TERM, 1939

In the Matter of the Reorganization of PITTSBURGH RAILWAYS
COMPANY, Debtor, and PITTSBURGH MOTOR COACH COM-
PANY, Subsidiary

No. 7271. Appeal of Tort Creditors' Committee

No. 7283. Appeal of City of Pittsburgh

And afterwards, to wit, the 6th day of March, 1940, come the parties aforesaid by their counsel aforesaid, and this case being called for argument sur pleadings and briefs, before the Honorable Albert B. Maris, Honorable William Clark and Honorable Charles Alvin Jones, Circuit Judges, and the Court not being fully advised in the premises, takes further time for the consideration thereof,

And afterwards, to wit, on the 30th day of April, 1940, come the parties aforesaid by their counsel aforesaid, and the Court, now being fully advised in the premises, renders the following decision:

[fol. 147] IN THE UNITED STATES CIRCUIT COURT OF APPEALS,
FOR THE THIRD CIRCUIT

Nos. 7271 and 7283. October Term, 1939

In the Matter of the Reorganization of PITTSBURGH RAILWAYS
COMPANY, a Corporation, Debtor, and PITTSBURGH MOTOR
COACH COMPANY, a Corporation, Subsidiary

Appeals of Tort Creditors' Committee and of City of Pitts-
burgh, Creditors

Appeals From the District Court of the United States, for
the Western District of Pennsylvania

OPINION—Filed April 30, 1940

Before MARIS, CLARK and JONES, Circuit Judges

MARIS, Circuit Judge.

These are appeals from an order of the District Court
for the Western District of Pennsylvania directing the

trustees of Pittsburgh Railways Company, a debtor in reorganization under Chapter X of the Bankruptcy Act and of Pittsburgh Motor Coach Company, a subsidiary, to pay as an administration expense taxes assessed against fifty-five underlying companies whose properties under lease and operating agreements form part of the Pittsburgh [fol. 148] Railways System. A schedule of the taxes involved in this appeal is set out below.¹

None of the taxes listed in the schedule was assessed against the debtor or its subsidiary and none bears any relation to the properties leased by the underliers to the debtor. Each is a tax upon the income of the underliers or upon their capital stock or securities. In other words, although they are taxes due and owing by the underliers to the state and federal governments, they are not taxes due and owing by the debtor. The sole obligation of the debtor with respect to these taxes arose under the leases and operating agreements with the underliers which provided that the debtor should pay all taxes assessed against the underliers.—The obligation of the debtor to pay the

¹ Unpaid balances of Federal Income Taxes of the underliers for the year 1937	\$97,412.14
Federal Income taxes for the year 1937 withheld at source in respect to interest upon the obligations of underliers	6,850.01
Pennsylvania Corporate Net Income taxes of the underliers for the year 1937	27,639.59
Federal Income taxes of the underliers for the year 1938	50,501.26
Federal Income taxes for the year 1938 withheld at source with respect to interest upon the obligations of underliers	2,668.08
Pennsylvania Corporate Net Income taxes of the underliers for the year 1938	18,335.72
Pennsylvania Capital Stock taxes of the underliers for the year 1938	64,294.57
Pennsylvania Corporate Loans taxes for the year 1938 in respect to interest upon the obligations of the underliers	17,502.56
Total	\$285,203.93

[fol. 149] taxes was an additional consideration for its use of the underliers' property, and, therefore, as to it a rental obligation rather than a tax liability.²

The appellees argue that since the properties of the underlying companies are in the possession of the trustees of the debtor and are being used and operated by them with properties of the debtor as a unified system the taxes of the underlying companies are, in effect, taxes of the unified system and are, therefore, operating and administrative expenses of the trustees.³ The district court adopted this view.

We are asked to ignore the legal relationships existing between the Philadelphia Company,⁴ the debtor and the underliers⁵ and their separate corporate identities and treat them all as one unified transportation system. For all practical purposes, the appellees argue, the separate identity of the underlying corporations has been lost. We are not impressed with the equity of this plea. Under other circumstances the appellee, the Philadelphia Company, has not sought to ignore its corporate identity but has taken refuge behind it to escape liability upon an underlier's

² Hardeman v. Hendrix, 29 F. 2d 738.

³ The trustees state:

"We do not contend these taxes are payable because the debtor contracted to pay them. While such contracts exist, thus far the Trustees have not affirmed them and may never do so. Whatever might be the effect of affirmance of the operating agreements and leases on the obligation of the Trustees to the underliers, we submit that the obligation of the Trustees to the taxing authorities is not governed by those contracts or by any action that might be taken by the Trustees with respect to them. Nor do we contend these taxes are payable as compensation for use and occupancy of the underliers' properties by the Trustees."

⁴ The Philadelphia Company is the holding company which owns all the stock of the debtor.

⁵ The debtor has an investment of approximately \$32,000,000 in the stock of the underliers.

[fol. 150] bond,⁶ as has also the debtor⁷ and an underlier.⁸ The appellees, the Philadelphia Company and the underliers, appear not too sincere in their contention that the corporate form is merely fiction when it is observed that the underliers have refrained from themselves filing petitions for reorganization, with the result that the only corporations in the system which are in process of reorganization are the debtor and its subsidiary. The Trustees are not trustees for the Philadelphia Company or for any of the underliers. Neither the past history of the system nor the present state of the reorganization proceedings would, we think, justify our ignoring the existence of the separate legal entities which compose that system.

A number of the taxes here involved became due prior to the filing of the petition for reorganization on May 10, 1938. These are the federal income taxes for 1937 and federal income taxes for 1937 withheld at source, due March 15, 1938⁹ and the Pennsylvania net income taxes for 1937, due April 15, 1938.¹⁰ Even though the taxpayer was given the option to pay these taxes in installments the taxes were actually due on the dates mentioned, which were the dates fixed by law for filing the tax returns. The failure of the debtor to pay these taxes was a breach of the leases and operating agreements and the amounts then due became simple contract claims against the debtor, due when the debtor's petition was filed.¹¹ As to these claims [fol. 151] the underliers must take their position with all other general creditors.

⁶ *Allen v. Philadelphia Co.*, 265 F. 807, affirmed 265 F. 817. Cf. *Ambridge Borough v. Philadelphia Co.*, 283 Pa. 5, 129 A. 67.

⁷ *Sec. Ave. T. Co. v. U. T. Co. & PBG.*, 328 Pa. 257, 195 A. 25.

⁸ *Lyon v. Pitts. A. & M. Tr. Co.*, 312 Pa. 584, 169 A. 229.

⁹ Revenue Act of 1936, c. 690, § 53, 26 U. S. C. A. § 53(a)1; Act of May 10, 1934, c. 277, § 143(c), 26 U. S. C. A. § 143(c).

¹⁰ Pennsylvania Act of May 16, 1935, P. L. 208, § 4, as amended, 72 P. S. § 3420(d).

¹¹ *Philadelphia & Reading Coal & Iron Co. v. Van Deusen*, 103 F. 2d 869.

A different question is presented by the taxes for 1938 since they became due while the trustees were actually administering the debtor's estate and making use of the properties of the underliers in such administration.

The trustees have no obligation to pay the rentals due under the leases, as such, unless and until they affirm the leases and operating contracts. They have a reasonable time within which to affirm or disaffirm. During the interim their sole obligation is to pay the lessors a reasonable amount for the use and occupation of the properties actually in use.¹² This rule, which was originally laid down in railroad receiverships in equity applies to the reorganization of a street railway under Section 77B of the Bankruptcy Act.¹³ If an interim payment is made it is ordinarily held that it should not be in an amount in excess of the net earnings derived from the operation of the lessor's properties.¹⁴

It may be, as argued by the appellees, that in this case it is impossible fairly to allocate the net earnings of the system to the various leased lines. In that case it may be necessary for the court to fix an allowance for use and occupation upon the basis of the fair value of the property actually used by the trustees. This we need not now determine for the court must first determine the property which is being used, the extent of its use and the net earnings being derived from it or its value.¹⁵ Until that is done any [fol. 152] order made by the court would have no factual basis and would, therefore, be arbitrary and possibly confiscatory.

It is urged that unless the taxes are paid immediately irreparable harm may result, since the taxing authorities may distrain. If and when this situation arises and the dis-

¹² *United States Trust Co. v. Wabash Railway*, 150 U. S. 287; *Pennsylvania Steel Co. v. New York City Ry. Co.*, 198 F. 721; *American Brake Shoe & Foundry Co. v. New York Rys. Co.*, 282 F. 523; *Westinghouse Electric & Mfg. Co. v. Brooklyn Rapid T. Co.*, 6 F. 2d 547.

¹³ *In re Connecticut Co.*, 95 F. 2d 311, cert. den. sub. nominee *Connecticut Railway & Lighting Co. v. Connecticut Co.*, 304 U. S. 571.

¹⁴ *Supra*—note 12.

¹⁵ *Public Service Commission v. Philadelphia Rapid T. Co.*, 82 F. 2d 481.

strict court deems such a distraint undesirable and likely to hinder the reorganization it may utilize the powers conferred upon it and enjoin all the proceedings to enforce the lien of any distraint made upon any property in which the debtor has an interest.¹⁶ However, the record before us does not justify a conclusion that the taxing authorities intend to distraint without leave of court. The court may properly withhold such leave pending determination of such vital questions to the reorganization as whether the trustees plan to affirm or disaffirm the leases, which of the underliers are to become part of the new transportation unit and whether the debtor's counterclaims against the underliers to which reference is made in the master's report are enforceable.

An impressive array of authorities is cited by the appellees to the effect that taxes are to be given preference in a proceeding such as this. We, however, are dealing with a contractual liability of the debtor, whereas in each of the cited cases¹⁷ the obligation was a genuine tax liability of the corporation itself and not as in the present case an obligation to pay the taxes of some other corporation.

The appellees give much weight to the fact that the trustees have in their possession funds derived, as they allege, almost wholly from the operation of the underliers' property, sufficient to pay all the taxes. They contend that [fol. 153] it is wasteful of the trust estate to permit interest and penalties to accumulate by reason of non-payment of these taxes. If, however, by reason of the ultimate disaffirmance of the leases the taxes should never become payable, as such, out of the debtor's estate and if the amount claimed as taxes should be found to exceed the sum justly due for use and occupation the trustees would be in error in so applying the funds in their possession. Furthermore the debtor may succeed in substantiating its claims against some of the underliers.

¹⁶ 11 U. S. C. A. §516(4).

¹⁷ *Michigan v. Michigan Trust Co.*, 286 U. S. 334; *Coy v. Title Guarantee & Trust Co.*, 220 F. 90; *Bear River Paper & Bag Co. v. City of Petoskey*, 241 F. 53; *MacGregor v. Johnson-Cowdin-Emmerich, Inc.*, 39 F. 2d 574; *Hardee v. American Security & Trust Company*, 77 F. 2d 382.

Enough has been said to demonstrate that the order of the district court cannot be sustained upon the record before us. It is accordingly

Reversed.

A true Copy. Teste:

— — —, Clerk of the United States Circuit Court
of Appeals for the Third Circuit.

[fol. 154] IN THE UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE THIRD CIRCUIT, OCTOBER TERM, 1939

No. 7271

In the Matter of the REORGANIZATION OF PITTSBURGH RAIL-
WAYS COMPANY, Debtor, and PITTSBURGH MOTOR COACH
COMPANY, Subsidiary

APPEAL OF TORT CREDITORS' COMMITTEE

Appeal from the District Court of the United States, for
the Western District of Pennsylvania.

This cause came on to be heard on the transcript of record
from the District Court of the United States, for the West-
ern District of Pennsylvania, and was argued by counsel.

On consideration whereof, it is now here ordered, ad-
judged, and decreed by this Court that the order of October
26, 1939 of the said District Court in this cause be, and the
same is hereby reversed; costs of this appeal to be paid out
of the Debtor's estate.

Philadelphia, April 30, 1940.

Albert B. Maris, Circuit Judge.

Endorsements: Order Reversing Order of Oct. 26, 1939
etc. Received & Filed Apr. 30, 1940. William P. Rowland,
Clerk.

[fol. 155] IN THE UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE THIRD CIRCUIT, OCTOBER TERM, 1939

No. 7283

In the Matter of the REORGANIZATION OF PITTSBURGH MOTOR
COACH COMPANY, Debtor, and PITTSBURGH MOTOR COACH
COMPANY, Subsidiary

APPEAL OF CITY OF PITTSBURGH

Appeal from the District Court of the United States, for
the Western District of Pennsylvania.

This cause came on to be heard on the transcript of record from the District Court of the United States, for the Western District of Pennsylvania, and was argued by counsel.

On consideration whereof, it is now here ordered, adjudged, and decreed by this Court that the order of October 26, 1939 of the said District Court in this cause be, and the same is hereby reversed; costs of this appeal to be paid out of the Debtor's estate.

Philadelphia, April 30, 1940.

Albert B. Maris, Circuit Judge.

Endorsements: Order Reversing Order of Oct. 26, 1939 etc. Received & Filed Apr. 30, 1940. William P. Rowland, Clerk.

[fol. 156] IN THE UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE THIRD CIRCUIT, OCTOBER TERM, 1939

No. 7271

In the Matter of the Reorganization of PITTSBURGH RAILWAYS COMPANY, Debtor, and PITTSBURGH MOTOR COACH COMPANY, Subsidiary

Appeal of Tort Creditors' Committee

ORDER VACATING DECREE

It is hereby ordered that the decree, or order of reversal, of this Court entered on April 30, 1940 be and the same is hereby vacated.

Philadelphia, June 12, 1940.

Albert B. Maris, Circuit Judge

Endorsements: Order vacating decree of April 30, 1940. Received & filed June 12, 1940. Wm. P. Rowland, Clerk.

[fol. 157] IN THE UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE THIRD CIRCUIT, OCTOBER TERM, 1939

No. 7283

In the Matter of the Reorganization of PITTSBURGH RAIL-
WAYS COMPANY, Debtor, and PITTSBURGH MOTOR COACH
COMPANY, Subsidiary

Appeal of City of Pittsburgh

ORDER VACATING DECREE

It is hereby ordered that the decree, or order of reversal,
of this Court entered on April 30, 1940 be and the same is
hereby vacated.

Philadelphia, June 12, 1940.

Albert B. Maris, Circuit Judge

Endorsements: Order vacating decree or order of April
30, 1940. Received & filed June 12, 1940. Wm. P. Row-
land, Clerk.

[fol. 158] IN THE UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE THIRD CIRCUIT, OCTOBER TERM, 1939

No. 7271

In the Matter of the Reorganization of PITTSBURGH RAIL-
WAYS COMPANY, Debtor and PITTSBURGH MOTOR COACH
COMPANY, Subsidiary

APPEAL OF TORT CREDITORS' COMMITTEE

Appeal from the District Court of the United States, for
the Western District of Pennsylvania

This cause came on to be heard on the transcript of record
from the District Court of the United States, for the West-
ern District of Pennsylvania, and was argued by counsel.

On consideration whereof, it is now hereby ordered, ad-
judged, and decreed by this Court that the order of October
26, 1939 of the said District Court in this cause be, and the
same is hereby reversed in so far as it directs the payment

of the taxes involved in this appeal; costs of this appeal to be paid out of the Debtor's estate.

Philadelphia, June 12, 1940.

Albert B. Maris, Circuit Judge.

Endorsements: Amended Order Reversing District Court Order of Oct. 26, 1939. Received & Filed. June 12, 1940. William P. Rowland, Clerk.

[fol. 159] IN THE UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE THIRD CIRCUIT, OCTOBER TERM, 1939

No. 7283

In the Matter of the Reorganization of PITTSBURGH RAILWAYS COMPANY, Debtor and PITTSBURGH MOTOR COACH COMPANY, Subsidiary

APPEAL OF CITY OF PITTSBURGH

Appeal from the District Court of the United States, for the Western District of Pennsylvania

This cause came on to be heard on the transcript of record from the District Court of the United States, for the Western District of Pennsylvania, and was argued by counsel.

On consideration whereof, it is now here ordered, adjudged, and decreed by this Court that the order of October 26, 1939, of the said District Court in this cause, be, and the same is hereby reversed in so far as it directs the payment of the taxes involved in this appeal; costs of this appeal to be paid out of the Debtor's estate.

Philadelphia, June 12, 1940.

Albert B. Maris, Circuit Judge.

Endorsements. Amended Order Reversing District Court Order of Oct. 26, 1939. Received & Filed June 12, 1940. William P. Rowland, Clerk.

[fol. 160] UNITED STATES OF AMERICA,

Eastern District of Pennsylvania,
Third Judicial Circuit, Sct.:

I, Wm. P. Rowland, Clerk of the United States Circuit Court of Appeals for the Third Circuit, do hereby certify

the foregoing to be a true and faithful copy of the original Transcript of Record and proceedings in this court in the matter of the Reorganization of Pittsburgh Railways Company, Debtor, and Pittsburgh Motor Coach Company, Subsidiary—No. 7271 Appeal of Tort Creditors' Committee, No. 7283 Appeal of City of Pittsburgh, on file, and now remaining among the records of the said Court, in my office.

In Testimony Whereof, I have hereunto subscribed my name and affixed the seal of the said Court, at Philadelphia, this 26th day of June in the year of our Lord one thousand nine hundred and forty and of the Independence of the United States the one hundred and sixty-fourth.

Wm. P. Rowland, Clerk of the U. S. Circuit Court of Appeals, Third Circuit.

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[fol. 161] SUPREME COURT OF THE UNITED STATES, OCTOBER
TERM, 1940

No. 242

ORDER ALLOWING CERTIORARI—Filed October 14, 1940

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Third Circuit is granted, and the case is assigned for argument immediately following No. 120.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

[fol. 162] SUPREME COURT OF THE UNITED STATES, OCTOBER
TERM, 1940

No. 243

ORDER ALLOWING CERTIORARI—Filed October 14, 1940

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Third Circuit is granted, and the case is assigned for argument immediately following No. 242.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

[Endorsed on cover:] File Nos. 44,591, 44,592. U. S. Circuit Court of Appeals, Third Circuit. Term No. 242. Philadelphia Company and Certain Underliers, Petitioners, vs. Walter L. Dipple, James P. McArdle, Ben Paul Brasley and Thomas J. Hoffman, etc., et al. Term No. 243. Philadelphia Company and Certain Underliers, Petitioners, vs. Walter L. Dipple, James P. McArdle, Ben Paul Brasley and Thomas J. Hoffman, etc., et al. Petition for writs of certiorari and exhibit thereto. Filed July 15, 1940. Term Nos. 242 O. T. 1940, 243 O. T. 1940.